S. HRG. 100-533

RURAL CELLULAR NON-WIRELINE LICENSING

HEARING

BEFORE THE

SUBCOMMITTEE ON COMMUNICATIONS

OF THE

COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION UNITED STATES SENATE

ONE HUNDREDTH CONGRESS

SECOND SESSION

ON

RURAL CELLULAR NON-WIRELINE LICENSING

JANUARY 27, 1988

Printed for the use of the Committee on Commerce, Science, and Transportation

U.S. GOVERNMENT PRINTING OFFICE

82-856 O WASHINGTON : 1988

5261-35

For sale by the Superintendent of Documents, Congressional Sales Office
U.S. Government Printing Office, Washington, DC 20402

COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION

ERNEST F. HOLLINGS, South Carolina, *Chairman*

DANIEL K. INOUYE, Hawaii
WENDELL H. FORD, Kentucky
DONALD W. RIEGLE, JR., Michigan
J. JAMES EXON, Nebraska
ALBERT GORE, JR., Tennessee
JOHN D. ROCKEFELLER IV, West Virginia
LLOYD BENTSEN, Texas
JOHN F. KERRY, Massachusetts
JOHN B. BREAUX, Louisiana
BROCK ADAMS, Washington

JOHN C. DANFORTH, Missouri
BOB PACKWOOD, Oregon
NANCY LANDON KASSEBAUM, Kansas
LARRY PRESSLER, South Dakota
TED STEVENS, Alaska
ROBERT W. KASTEN, JR., Wisconsin
PAUL S. TRIBLE, JR., Virginia
PETE WILSON, California
JOHN MCCAIN, Arizona

RALPH B. EVERETT, *Chief Counsel and Staff Director*
WALTER B. MCCORMICK, JR., *Minority Chief Counsel and Staff Director*

SUBCOMMITTEE ON COMMUNICATIONS

DANIEL K. INOUYE, Hawaii, *Chairman*

ERNEST F. HOLLINGS, South Carolina
WENDELL H. FORD, Kentucky
ALBERT GORE, JR., Tennessee
J. JAMES EXON, Nebraska
JOHN F. KERRY, Massachusetts

BOB PACKWOOD, Oregon
LARRY PRESSLER, South Dakota
TED STEVENS, Alaska
PETE WILSON, California
JOHN MCCAIN, Arizona

CONTENTS

	Page
Opening statement by Senator Inouye	1
Opening statement by Senator McCain	2
Opening statement by Senator Pressler	3
Opening statement by Senator Adams	20

LIST OF WITNESSES

Blum, Thomas C., general manager, external affairs, Bell Atlantic Mobile Systems, Inc	82
Prepared statement	84
Questions of Senator Pressler and the answers	86
Brock, Gerald, Chief, Common Carrier Bureau, FCC; accompanied by Kevin Kelly	3
Prepared statement	6
Questions of Senator Pressler and the answers	10
Henry, E. William, on behalf of the U.S. Independent Cellular Telephone Assn	46
Prepared statement	47
MacLeod, William C., Director, Bureau of Consumer Protection, FTC	11
Prepared statement	12
Maher, Robert, president, Cellular Telecommunications Industry Assn	67
Prepared statement	69
Questions of Senator Pressler and the answers	72
McAllister, John, president, West Carolina Rural Telephone Cooperative	73
Prepared statement	75
McCaw, John E., Jr., executive vice president, McCaw Communications	35
Prepared statement	36
Questions of Senator Pressler and the answers	44
Neff, H. Robert, president, Cellular of Northwest Ohio	26
Prepared statement	28
Seltzer, Steven S., president, Modern Communications Corp	52
Prepared statement	54
Stroup, Thomas A., vice president, Telocator Network of America	77
Prepared statement	79

ADDITIONAL ARTICLES, LETTERS, AND STATEMENTS

American Cellular Engineering Assn., statement	100
Batsche, George M., president, Communications Transmission, Inc., statement	93
Bolter, Walter G., Ph.D., CPA, director, Bethesda Research Institute, Ltd., statement	95
Bowers, Steven G., chief engineer and vice president, Moultrie Independent Telephone Co., statement	91
Brunner, Michael E., executive vice president, National Telephone Cooperative Assn., letter	121
Curtis, Clayburn C., president ACRS, Inc., letter	106
D. B. Communications, Inc., statement	102
Fox, Russell H., executive director, American SMR Network Assn., Inc., letter	113
Guthrie, Michael T., CellTek, letter	124
Healy, Robert W., letter	123
Lhu, Leo Buk, editor, Celintel Newsletter, and manager, Cellular Computing Database, statement	92
Minnesota Telephone Assn., statement	92
Morrow, Bud L., president, Lakedale Telephone Co., letter	120
Patrick, Hon. Dennis, R., Chairman, FCC, letter	105
Seminole Tribe of Florida, letter	108
Telephone and Data Systems, Inc. and U.S. Cellular Corp., letter	115
Umetsu, Glenn T., president & general manager, Honululu Cellular Telephone Co., letter	125
Watson, Denny P., president, Mobilcom, letter	118

RURAL CELLULAR NON-WIRELINE LICENSING

WEDNESDAY, JANUARY 27, 1988

U.S. SENATE,
SUBCOMMITTEE ON COMMUNICATIONS,
COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION,
Washington, DC.

The subcommittee met, pursuant to notice, at 9:00 a.m., in room SR-253, Russell Senate Office Building, Hon. Daniel K. Inouye (chairman of the subcommittee) presiding.

Staff members assigned to this hearing: John Windhausen; Tom Cohen, staff counsels; and Gina Keeney, minority staff counsel.

OPENING STATEMENT BY SENATOR INOUYE

Senator INOUYE. This morning we will discuss the FCC's way of awarding licenses to operate cellular telephone systems. In particular, we will explore the pros and cons of the FCC's plan to use a lottery to award the non-wireline licenses to operate cellular systems in the rural areas. We will also discuss proposals to change or improve upon the lottery process. Our goal is to ensure that these rural licenses are granted only to those who will expeditiously provide competitive service to the American public.

The FCC used lotteries to issue the majority of the metropolitan cellular licenses in 1986. Because these lotteries were open to everyone, speculation in these licenses was rampant. We will hear this morning how thousands of individuals applied to win these licenses, not to build and own a cellular system, but solely to reap a financial windfall.

In the year and a half since the last metropolitan lottery, well over half of the lottery winners have sold their licenses for millions of dollars to existing cellular companies. As a result, the public has suffered from delayed service and unnecessary costs.

The lotteries have also led to fraud, and marketing firms have sold thousands of applications to the public, advertising the lotteries as an investment opportunity of a lifetime. Even where fraud has not been proven, the activities of many of the firms marketing cellular applications appear to cross the limits of proper business practice.

At the same time, there were applicants in the lottery who were not in the communications business but who were nevertheless financially qualified and sincere in their desire to provide service. We will hear this morning from a businessman who won a license and who constructed his own system in a metropolitan area.

The FCC is planning to begin awarding the licenses to serve rural areas in several months. By planning to use an open lottery

for these rural licenses, the FCC has admitted that it cannot discriminate between qualified applicants and speculators.

The purpose of this hearing is to determine if Congress can craft a better solution to this problem. While this is an issue of first impression for this subcommittee, this process may set a precedent for licensing new services in the future.

Obviously our overriding goal is to make high quality competitive service available to the public. This goal is especially important in the rural areas where many residents still do not have access to basic telephone services. To reach this goal we must face our responsibility to ensure that the non-wireline cellular licenses are awarded to qualified applicants. There is no guarantee that we will be able to find a solution in this morning's hearings, or even afterwards, and even if a solution does appear reasonable, we must be certain that it will not delay the availability of this valuable service to the public.

Cellular technology has been available since the early 1970s, awaiting regulatory approval. We will have abandoned our responsibility to the public if we add to this delay.

This morning we have several panels, and our first panel consists of Mr. Gerald Brock, Chief of the Common Carrier Bureau of the Federal Communications Commission, and William C. MacLeod, Director, Bureau of Consumer Protection, the Federal Trade Commission.

Senator McCain.

OPENING STATEMENT BY SENATOR McCAIN

Senator McCAIN. Thank you, Mr. Chairman. I appreciate you holding this hearing. I think it is a very important one. It is not a high visibility issue, but it is clear that it is one of intense interest to those who are involved in this issue.

Cellular communications, no doubt, is a cutting edge technology, and it is an area of opportunity for small businessmen and entrepreneurs throughout this country. I know that the reason for this hearing is that we are concerned about how this technology, indeed, this opportunity is made available to the public.

I believe in the concept of a nationwide cellular network, and I believe it should be in place as expeditiously as possible. I myself, Mr. Chairman, as I know you have, have made use of this technology many times, to the regret of my staff who used to feel that they were safe when I was in an automobile.

However, we must use care in pursuing these goals, and we must not trammel the rights of individuals as we seek to accomplish these goals. And Mr. Chairman, I can see no reason why, as we give out remaining metro and the rural licenses, those who were fortunate enough to receive a license earlier should get any advantage in seeking the remaining licenses.

I do not approve of the speculation that has occurred in these earlier cases, and I believe that we should try to prevent that in the future, perhaps by demonstration of capability, both financial and technologically, being required for those who receive these licenses, somewhat along the lines as the way we distribute mining licenses.

I think this can be done, and in addition, by using FTC and others, we can police the problems that have arisen in these so-called application mills.

Thank you, Mr. Chairman, and I again apologize for not being able to be here through the entire hearing. As a member of the Armed Services Committee, we are considering the INF treaty, and I am going to have to leave. But I think this is a very important hearing, and I am sure we will be hearing a lot more on this issue.

Thank you, Mr. Chairman.

Senator INOUYE. Thank you, Senator McCain.

Senator Stevens.

Senator STEVENS. Mr. Chairman, I congratulate you, too, for holding the hearing. We are vitally interested in this subject in Alaska. But I have no opening statement.

Senator INOUYE. Senator Packwood.

Senator PACKWOOD. No opening statement. Thank you, Mr. Chairman.

Senator INOUYE. I have a statement that Senator Pressler would like included in the record.

[The statement follows:]

OPENING STATEMENT BY SENATOR PRESSLER

Mr. Chairman, I will make just a brief statement.

Once again, those of us in rural America are waiting for a new technology to be taken off hold. This hearing is extremely important in determining how rural America will gain access to cellular technology, and I am pleased that it was scheduled so promptly. I am hopeful that we can come to a consensus quickly and see the development of cellular systems soon in the rural areas of this country.

The issue before us is how to prevent speculation in cellular licensing. While the objective is admirable, some of the proposals for accomplishing it are not without problems. They would eliminate legitimate competition for the sake of preventing speculation. There is such a thing as over-reacting, and we must be careful that we don't fall into that trap.

I am especially concerned about the proposal to limit rural service area [RSA] applicants to those currently holding metropolitan service area [MSA] licenses. There are a number of other, less drastic approaches to this problem. These include prohibiting profits from the sale of permits, setting construction time limits, and requiring operation of a system for a period of time prior to selling it. These approaches would limit speculation, but still allow legitimate parties to get involved in the process.

Senator INOUYE. Before proceeding, I would like to note that at this moment, representatives of opposing interests are meeting to come forth with a consensus agreement on how to resolve this matter, and I would like to encourage that movement because if the word is not received from the industry, the FCC might find itself doing its thing, and I think all of us would suffer accordingly.

Mr. Brock.

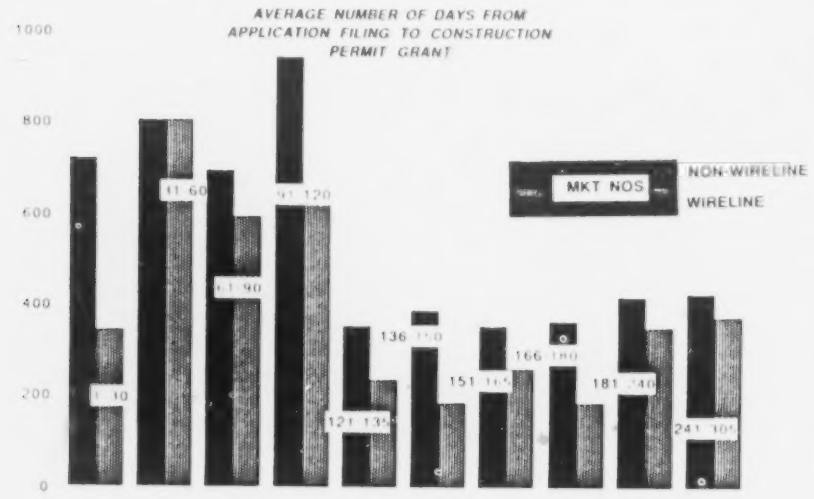
STATEMENT OF GERALD BROCK, CHIEF, COMMON CARRIER BUREAU, FEDERAL COMMUNICATIONS COMMISSION, ACCOMPANIED BY KEVIN KELLY

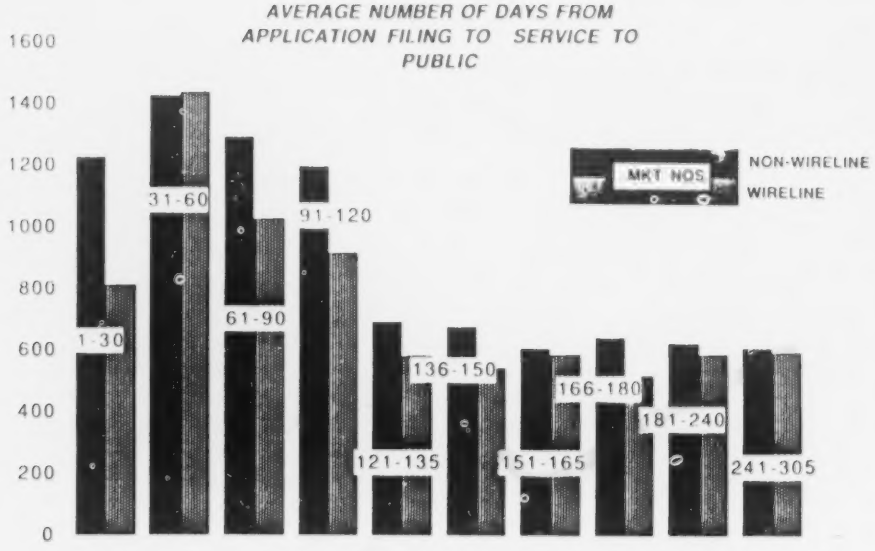
Mr. BROCK. Thank you, Mr. Chairman. I appreciate the opportunity to present the FCC's views before you this morning. My prepared statement contains a considerable amount of detailed statistical material on our experience so far with the licensing process, and I would like to ask that it be incorporated into the record.

Senator INOUYE. Without objection, your statement will be made part of the record.

Mr. BROCK. This morning I would like to summarize that material with the aid of this chart.

[The chart follows:]





Mr. BROCK. This chart shows the total time from application to final service date for each of our groups of markets under the metropolitan service area arrangements. The solid bar is the time required for non-wireline licenses; the shaded bar is the time required for wireline licenses.

We have used four different sets of procedures in preparing the 305 metropolitan service areas, including comparative hearings in markets 1 through 30, and different methods of a lottery process in the remaining markets.

We have received, as you noted in your opening statement, a very large number of applications in the later markets, increasing from an average of approximately five applications per non-wireline market under the comparative hearing process, to approximately 500 per non-wireline market in the later markets. However, as we have refined the lottery process, we have been able to improve the speed of service, bringing it down to, in the later markets, an average of approximately one year between the filing of an application and the grant of a construction permit, and one more year between the construction permit and the beginning of service to the public.

The refinements have also narrowed the difference between wireline and non-wireline speeds. At present, it requires slightly more time to grant a construction permit for the non-wirelines, but the non-wirelines are slightly faster in actually building the facilities, so that the speed of service from the original application until final service is approximately the same.

We have incurred a number of problems, as you mentioned, in this process, including a large number of speculators, raising some questions about the sincerity of applicants. However, we have not wavered in our commitment that only sincere applicants who seriously intend to build a system should be allowed into this process.

When we receive an application to transfer, if we have reason to believe that it was initiated purely for speculation, we will refuse that permission.

As we turn to licensing in rural service areas, we have planned a number of further refinements to this process in order to reduce speculation and to speed up the process. These consist of three different areas.

The first is that we have proposed to prohibit partial settlement arrangements or alliances among groups. These arrangements have been used by promoters to encourage nonserious applicants to apply with the promise that they would be relatively certain to get some part of an application. We are also proposing to strengthen the financial requirements and therefore make it more difficult for those who are not serious to apply. In addition, we are continuing to refine our processing procedures and produce faster service to the public.

Our current schedule, subject to any modifications that may be made or suggested by this committee, calls for accepting all rural service applications during calendar year 1988 and holding lotteries during the same calendar year for those applications.

Thank you, Mr. Chairman.

[The statement follows:]

STATEMENT OF GERALD BROCK, CHIEF, COMMON CARRIER BUREAU, FEDERAL COMMUNICATIONS COMMISSION

Good morning Mr. Chairman and members of the Committee. Thank you for giving the Federal Communications Commission this opportunity to discuss the methods and procedures it plans to use to accept and process applications to provide Cellular Radio Service in rural areas. These activities are part of the Commission's ongoing efforts to bring the benefits of cellular radio to all Americans as expeditiously as possible. Before discussing the specifics of the Commission's plans, let me describe first the Commission's experience in processing the Metropolitan Statistical Area (MSA) applications.

In 1974 the Commission allocated 40 MHz of spectrum for Celluar Radio. It decided that because of the complex technical nature of the service, the high cost of building the facilities, and the spectrum efficiency concerns surrounding the service, it would not be advisable to license competing systems. Moreover, it concluded that because wireline companies (telephone carriers) were in the best position to provide this service, only they would be licensed. The following year the Commission amended this latter determination deciding that it was unfair and discriminatory to allow only wireline companies to be licensed.

In 1981, after granting developmental authorizations in Chicago and the Baltimore/Washington markets, the Commission amended its earlier decisions and concluded that facilities based competition would best serve the public interest. Thus, it adopted rules for licensing two Cellular Systems in each market with each system being allocated 20 MHz of spectrum. One of the allocations was reserved for wireline carriers, certificated in the market for which they were applying, and the other allocation was available to any qualified entity. The Commission did consider the use of auctions or lotteries but because it did not have the statutory authority, the only practical course of action was to use comparative hearings to select from among competing applicants.

In June of 1982 the Commission received applications for markets 1 through 30. It received 52 wireline applications and 141 non-wireline applications.[1] In all the wireline markets the applicants either reached a full market settlement or only one applicant had filed for a particular market and thus, no hearings were necessary. The average time between the receipt of the wireline applications and the granting of a construction permit was 343 days. For the non-wireline markets, comparative hearings were held in 24 markets. The average time between the receipt of the non-wireline applications and the grant of a construction permit was 720 days. Of course, most of this processing time was a result of the lengthy comparative hearings.

In 1983, after conducting several hearings, the Commission concluded that the hearing process had not uncovered substantial differences among the competing applicants and that virtually all applicants were fully qualified to construct and operate a cellular radio system. It was also around this time that the Commission had received authority from Congress to use lotteries. Consequently, the Commission decided to award the remaining cellular authorizations using lotteries, including, I might add, those applications that had already been filed for the next 60 markets (markets 31 through 90). In these markets, 154 wireline applications and 765 non-wireline applications were filed. Again, all of the wireline markets were settled or only one applicant had applied for a particular market. Also, in all but three non-wireline markets the applicants had reached a full settlement and thus only three lotteries were necessary.

At the time it adopted the technical lottery procedures, the Commission also adopted new qualification standards for the remaining markets. These standards included strict service area coverage requirements, financial standards and a variety of technical qualifications. Moreover, the Commission allowed the use of "cumulative chances" in the lottery process. This technique permitted the formation of settlement groups that had as many chances of winning a particular market as there were members in each group. The Commission decided to allow cumulative chances because of the essential role cumulative chances could play in promoting full market settlements and thereby expediting the provision of service to the public. The Commission stated that the settlement process could shorten the time it would otherwise take to authorize cellular service in these areas. The Commission also expressed confidence that, regardless of the method selected, hearings or lotteries, it

[1] Statistical summaries, from the Commission's cellular radio data base, used to prepare this testimony are included as attachments. The attachments were not reproducible and are in the Committee files.

could ensure that the public would receive high-quality cellular service and that the additional qualification standards would act as a barrier to frivolous applicants.

The Commission did not immediately recognize, however, that under its lottery selection procedures, some applicants might file mass-marketed, non-exclusive cellular applications and thereby gain inexpensive entry into the lotteries for the remaining 215 markets. After the first filing under lottery procedures, when this practice became evident, the Commission stated that while such applications were not *per se* unacceptable, it cautioned prospective applicants that mere "Lottery Tickets" would not be accepted for filing. To be acceptable, a cellular application had to clearly demonstrate the applicant's technical and financial qualifications and demonstrate why the grant of the application would serve the public interest. Finally, the Commission amended its cellular anti-trafficking rules to make them similar to the rules applicable to conventional mobile radio and low power television services. The Commission believed it had struck a balance between the need to promote the efficient use of the spectrum by allowing increased transferability of licenses and the necessity to deter insincere applicants.

In markets 91 through 120, the first group of markets in which applicants knew there would be a lottery, the Commission received 98 wireline applications and 3,882 non-wireline applications. The average time between the filing of a wireline application and the grant of a construction permit was 636 days. The average for a non-wireline application was 941 days. The primary reason why it took so long to process the applications was the inordinate amount of staff time required to review carefully each application before the lottery.

After its experience with markets 91 through 120 the Commission again modified its procedures because of a variety of schemes that were being used by application preparers to increase the chances of an applicant or a group of applicants to win a lottery. First of all, the Commission did away with cumulative chances for non-wireline applicants since the sheer number of applicants effectively prevented full market settlements.[2] Second, the Commission changed its financial requirement standards from a "reasonable assurance" standard to a "firm financial commitment" standard. The first financial commitment standard requires that the applicant either has the necessary cash to construct and operate its system for one year or can prove the existence of a firm financial commitment from a bank or other financial institution.

The Commission also amended various filing and processing procedures to reduce and streamline the process. For example, the process of reviewing all applications prior to the lottery was replaced with a self certification procedure and full scrutiny was applied only to the winning application. Further, the Commission changed the financial requirement procedures so that only the Tentative Selectee needed to meet the new firm financial commitment standard. This change was made because applicants indicated that the high cost associated with obtaining a firm financial commitment would draw substantial capital away from the construction, system development, and subsequent operation of a cellular system.

In markets 121 through 305 the Commission accepted applications in a series of filing rounds of 15 to 25 markets each. These applications were filed between February 3, 1986 and May 23, 1986. Ten lotteries were held between April 21, 1986 and December 15, 1986. In these 185 markets the Commission received 93,033 non-wireline applications and 563 wireline applications. A total of 95 Petitions to Deny were filed, 77 against the non-wireline winners and 18 against the wireline winners. To judge how effective the Commission's amended rules and procedures were in handling the large increase in applications, it is useful to compare, by market groups, the average time between the application filing date and the granting of construction permits. As I indicated earlier, the average time for non-wireline markets varied from 720 days for markets 1 through 30 to 941 days for markets 91 through 120. With the new rules and procedures, the average time between receiving applications and granting construction permits varied between 353 days for markets 121 through 135, to 422 days for markets 241 through 305. The Commission's adjustments, as it gained experience with the evolving market and its own procedures, reduced significantly the amount of time it had taken to get this service to the public. Of course, the granting of construction permits only measures how fast the Commission was able to process the applications. From a public service point of view, the number of days between granting the construction permit and instituting service to the public is equally important. For non-wireline markets the average was

[2] Cumulative chances were kept for wireline applicants because there was no evidence that there had been a problem with these applicants and full market settlements had been reached in most markets.

507 days for markets 1 through 30 and is 184 days for the licenses which have been granted in markets 241 through 305. Thus, the average time from filing non-wireline applications to actually providing service to the public has decreased from 1,227 days, in markets 1 through 30, to 606 days for markets 241 through 305.

As of January 21, 1988 the Commission has granted 300 of the 305 possible wireline construction permits. The remaining five wireline markets have not received construction permits because there is still a pending petition to deny in one market, the winning application was returned as defective in another, a multi-market settlement is currently under review in another and there were no wireline applications filed in the other two markets.[3] Finally, of the 300 wireline permittees, 197 have completed initial construction and are offering service to the public.

Furthermore, the Commission has granted 271 of the 305 possible non-wireline construction permits. Of the remaining 34 non-wireline markets 18 are being investigated for possible lottery irregularities and 16 are still pending for a variety of reasons including pending petitions to deny, implementation of hearing settlement agreements and the reprocessing of markets where the original lottery winner was rejected. Nevertheless of the 271 non-wireline permittees, 116 have completed initial construction and are offering service to the public.

In summarizing our experience in accepting and processing applications in MSA markets, I think the Commission responded quickly to the changing conditions it encountered as it attempted to bring a new radio service to the public as quickly as possible. Certainly there were and are problems but the essential facts are that cellular radio service is now available from 313 different cellular radio systems and more than 1,000,000 Americans are no using the service.

I would like to discuss briefly the transfers and assignments of cellular radio authorizations. The charge has been made that many non-wireline applicants are selling their grants as soon as they receive them from the Commission.[4] The Commission has received, as of January 1, 1988, 115 requests for authority to transfer or assign non-wireline authorizations. The Commission has also received 29 wireline transfer requests. The fact there have been more non-wireline transfer requests is a result of the changing nature of the cellular industry and the types of operators involved. For the most part, the wireline carriers are large well financed corporations and usually have authorizations in several adjacent markets. The non-wireline carriers, on the other hand, are frequently small corporations or individuals who, although qualified to build and operate a system are, in some cases, finding it difficult to react in this dynamic new industry. Some of the requests for transfers and assignments represent exchanges of facilities between carriers. Others represent purchases of non-wireline systems by Regional Bell Operating Companies and still others represent purchases by non-wireline carriers that are attempting to build regional systems. The Commission believes that the large number of non-wireline transfer requests represent, for the most part, a natural response to the evolving cellular industry structure rather than any lack of sincerity on the part of the applicants. It should be emphasized that the majority of the non-wireline authorizations have not been transferred and that many small non-wireline systems have been or are being constructed and the operators of these systems expect to offer robust competition to the wireline carriers.

I will now summarize the status of our rural licensing preparations. The Commission had originally thought that it would be best to allow those wanting to provide rural cellular service to define their own service areas. However, the public expressed the view that this would result in a long and confusing licensing process and the public would be better served if the Commission adopted fixed boundaries for these areas. As a result, in 1986 the Commission adopted a system of defined Rural Service Area (RSA) boundaries based on a plan submitted by United Telespectrum. There were approximately 425 RSAs defined in the Commission's original RSA Order. Currently, the Commission is preparing to issue its second Order on Reconsideration involving the RSA boundaries. This Order should resolve remaining disputes among potential RSA applicants and finalize appropriate boundaries for the contested areas. To facilitate the accepting of RSA applications, the Commission divided the RSAs into 5 regional groups each containing approximately 75 rural markets. A lottery was held to determine the order in which applications for each of

---

[3] The Commission again accepted applications for these two markets earlier this month and received 3,195 applications.

[4] Of course no authorization can be transfered without prior Commission approval and before approving any transfer request the Commission carefully reviews both the qualifications of the proposed transferee and the motivation of the transferor.

these regional groups would be accepted for filing. The Commission has not yet decided on specific lottery procedures for selecting winners in each market.

The Commission has proposed further rule changes to avoid problems it encountered in the final MSA processing rounds. One proposal was to restrict the applicability of the so called one percent rule for non-wireline applicants. The one percent rule precludes an applicant from having a one percent or greater ownership interest in more than one application in a particualr market. The proposal would prevent any ownership interest in more than one application in a particular market. This restriction would not apply to publicly traded companies. The result of this and other changes would be to ban all non-wireline partial settlement groups including the so called "alliances" that were used in markets 121 through 305. "Alliances" are, in fact, agreements among some applicants in a market which provide that if any member of the alliance won the lottery that member would retain a majority ownership interest in its application and the other members of the alliance would divide the remaining interest equally. It further provided that each minority owner would receive less than a one percent interest. The Commission made this proposal because it had concluded that non-wireline partial settlements did not reduce the need to hold lotteries and also caused delays in the granting of applications. Furthermore, these agreements involved the Commission in disputes among the members of the settlement groups thereby further delaying the processing of the applications. As Chairman Patrick mentioned in his letter to Chairman Hollings, the Commission expects to take action on these items within the next two months and will also consider the appropriate financial qualifications standards that will be applicable to RSA applicants.

The Commission is pleased to work with the Congress as it analyzes whether legislation or other action is appropriate to discourage speculative applications in the RSAs. Measures that have been suggested to accomplish this result include increased application filing fees, imposition of substantial grant fees, tightening financial qualifications standards, and restricting filing eligibility to entities that have a cellular or radio common carrier presence in the area.

From the last round of MSA filings, it is clear that the current $200 application filing fee will not result in any significant reduction in the number of applications filed. In our view, a significant increase in the filing fee and a substantial grant fee, reflecting the high value of a cellular radio license, would discourage speculative filings by reducing the potential windfall again. We are also considering changes in our required financial qualification showing to ensure that applicants have the ability to implement a system if they are selected.

We have serious reservations about proposals to restrict eligibility for RSA applicants to entities which are already providing common carrier radio service in or near the area, as some MSA licensees have proposed. While this would certainly eliminate virtually all speculative filing, it is so restrictive that it raises issues of fundamental fairness. The open entry policy has allowed many new individuals to enter the cellular radio business, bringing new ideas and technological innovation to invigorate the industry. Serious applicants which are not already common carrier licensees would be excluded by some of the restricted eligibility proposals. The complexity of some of these proposals may result in delays in licensing or legal challenges, either of which would delay ultimate service to the public.

I welcome the opportunity to discuss these and other measures that the Commission might take to ensure that cellular service is provided to all Americans. I believe that by using the procedures and experiences that the Commission has developed during the MSA filings, refined through the current notices of proposed rulemakings and input from this Committee, the Commission will be able to process RSA applications more rapidly than it processed the MSA applications. This will ensure our mutual goals of getting reliable high quality service to the public and doing so in the most expeditious and competent manner.

[The following information was subsequently received for the record:]

QUESTIONS OF SENATOR PRESSLER AND THE ANSWERS THERETO

Question (1) -- What specific changes does the FCC plan to implement to reduce speculation in the Rural Service Area lotteries?

The Commission will be identifying specific solutions to the speculation problem in the course of its Rural Cellular rulemaking proceedings. Athough that proceeding has not been completed, the Commission has under consideration a number of proposals. First, the Commission is considering a prohibition against partial settlements among non-wireline applicants. In the selection process for Metropolitan Service Area licenses, applicants entered into settlement agreements in order to enhance their chances of obtaining an interest in a cellular license through the lottery. Thus, the Commission is considering whether, if partial settlements are prohibited, speculators would be less likely to participate in the lottery because the chances of obtaining a cellular interest would have diminished.

The Commission is also considering elimination of the so called 1% rule. Although applicants have been prohibited from having an ownership interest in more than one application per market, interests of less than 1% are allowed. The 1% exception allowed applicants to form settlement groups. Elimination of the 1% exception would mean that an applicant could not offer minority interests in its application to other filers and would eliminate the loophole that provided a basis for settlements. Again, adoption of this provision would make speculation in cellular applications far more risky and could dissuade speculators from filing.

Question (2) Do you have any alternative proposals for limiting speculation without eliminating serious competitors or putting undue burdens upon their involvement?

Consideration is being given to modifying the financial showing required of RSA applicants. Currently, only the lottery winner is required to demonstrate that it has a firm financial commitment to provide the funds necessary to construct and operate its proposed cellular station. The Commission is considering the idea of requiring all RSA applicants to demonstrate their financial ability at the time their applications are filed. A more stringent financial showing may have the beneficial effect of eliminating speculators who would be unable or unwilling to obtain the necessary financial backing.

Question (3) Which of the various proposals being advocated could be implemented without a new rule-making procedure?

Only modification of the financial showing would require a new rule-making. The Commission released a Third Notice of Proposed Rulemaking on financial showings on February 19, 1988. The provisions mentioned in the answer to Question 1 are being considered in on-going proceedings.

Question (4) If high filing fees are required for RSAs, how will rural independent telephone companies be allowed to compete?

As you may be aware, only Congress can readily alter the FCC fee structure. If Congress does decide to increase significantly the RSA filing fee for both wireline and nonwireline applicant, there may be some rural independent telephone companies that would not be able to afford the new fees. Such companies may nevertheless be able to file an application by entering into agreements with other RSA eligibles to file a combined application.

Question (5) If the filing the fees are only raised for non-wireline companies, what assurance is there that FCC, in the name of fairness, will not extend the requirement to wirelines?

As noted above, only Congress can change the filing fees. If Congress makes such a change for non-wirelines only, the Commission would be unable to require such a fee from wirelines.

Question (6) Why does the FCC allow "cookie-cutter" applications for the lotteries?

After conducting several comparative hearings, the Commission concluded that the hearing process had not uncovered substantial differences among the competing applicants and that virtually all applicants were fully qualified to construct and operate a cellular radio system. After the first filing under lottery procedures, when the practice of filing mass-marketed, non-exclusive cellular applications were not per se unacceptable, it cautioned prospective applicants that mere "lottery tickets" would not be accepted for filing. It is, in large part, in response to those mass-marketed applications that the Commission has proposed requiring firm financial showings at the time the applications are filed.

Senator INOUYE. Thank you very much.
Mr. MacLeod.

STATEMENT OF WILLIAM C. MacLEOD, DIRECTOR, BUREAU OF CONSUMER PROTECTION, FEDERAL TRADE COMMISSION

Mr. MACLEOD. Thank you, Mr. Chairman, Members of the subcommittee. I would like to summarize my statement and submit the written statement for the record, if I may.

Senator INOUYE. Without objection, your full statement is made a part of the record.

Mr. MACLEOD. Thank you.

Mr. Chairman and members of the subcommittee, my name is William MacLeod, and I am the Director of the Bureau of Consumer Protection at the Federal Trade Commission. I appreciate the opportunity to appear before the subcommittee today on behalf of the FTC to discuss our activities in connection with the marketing of cellular telephone licenses.

What we saw in this industry was the birth of a relatively new industry of application preparation services. These were firms that offered to provide customers with engineering, legal, demographic and financial planning expertise necessary to complete the comprehensive and detailed application required under the lottery. As with many goods and services and sales to the public, the potential for deception exists, and that potential for deception occasionally was realized here.

Today I will describe the fraudulent practices that dishonest firms selling these services have actually engaged in and describe the measures that the Federal Trade Commission has taken to combat these practices.

We discovered that firms using these practices, these marketers of application services, typically use telephone boiler rooms, as we call them, to market their wares. Typically there would be advertisements in newspapers and television or radio, and these advertisements would be followed up by a sales force on the telephone to tell customers that should they apply, they would be very rich, that they had high chances of winning the lottery should they apply. They charged significant prices, much greater prices than the actual application fee charged by the FCC in order to service the application. They use slick brochures, detailed charts and graphs showing profit projections and maps of geography and so on to give a bona fide look to a pitch that essentially a customer was getting a very valuable and relatively low risk investment.

There was a good deal of high pressure sales going on in this industry. Very often the salesmen would tell customers they had to act quickly in order to get in under the deadline of a particular lottery, when in fact the date for the lottery had not even been set by the FCC as yet. And these pitches were successful.

There were a number of victims across the land, running the gamut from sophisticated investors to doctors, engineers, folks with retirement money. These were people looking for an investment, looking for a return on their investment. Very often, consumers who purchased applications would be encouraged to purchase addi-

tional applications, and consumers would often be into these services for thousands and sometimes tens of thousands of dollars.

The Commission's response to this has been the response that the Commission has made to any number of activities that we have seen of this kind. This is not something unique that we have discovered with lotteries for licenses for cellular telephones. We have seen the same kind of practices with respect to the marketing of rare coins, with respect to the marketing of rare gems, with respect to the marketing of a number of valuable goods or services that consumers find in great demand.

I think of the old words of the famous bank robber who said, "Why did he go to the banks? That's where the money was." There is a valuable resource being made available to the public here. That resource gave the opportunity for individuals marketing the resource to describe it as even a little more valuable to the individual consumer than it actually was. That is where the FTC moved in.

We moved in to stop the deceptive claims that were being made, and indeed, we stopped the two largest application services from making their deceptive claims. We put individuals and corporations under court order. We have secured approximately $1 million in redress for the victims. More than 3,000 victims will be receiving redress checks in April or May of this year as a result of these actions. And I am not even counting the actions that we have taken in court to secure criminal contempt convictions against some of the defendants who did not comply with the court orders originally.

In addition, I think that it is useful to describe some of the activities that the Commission has been engaging in with the cooperation of the FCC as well as state and local authorities. This has been a cooperative law enforcement effort. We have set up computer exchange networks for the exchange of information. We have received a great deal of cooperation from the FCC and state attorneys general around the country as well as securities administrators around the country to help us get a handle on and put an end to some of the fraudulent practices that we have seen in the business.

In conclusion, the Commission shares the subcommittee's concern about the problems engendered by the process to award licenses to build and operate cellular telephone systems. While the lottery system has enabled ordinary citizens to own cellular licenses, many more consumers have been misled and defrauded by scam operators who have taken every advantage to abuse the lottery process.

We are continuing our work to put the worst actors out of business, and we are encouraged by the subcommittee's efforts to join us in the battle.

Thank you, Mr. Chairman. That concludes my summary.

[The statement follows:]

STATEMENT OF WILLIAM MACLEOD, DIRECTOR, BUREAU OF CONSUMER PROTECTION, FEDERAL TRADE COMMISSION

Mr. Chairman and members of the Subcommittee: My name is William MacLeod, and I am Director of the Bureau of Consumer Protection at the Federal Trade Com-

mission. I appreciate the opportunity to appear before you today on behalf of the Federal Trade Commission to discuss our activities in connection with the Federal Communications Commission's lottery for cellular telephone licenses.

In 1984, the Federal Communications Commission decided to hold lotteries to award licenses to build and operate cellular telephone systems in the United States. Prior to this decision, licenses were awarded following lengthy public hearings during which each applicant sought to establish its technical and financial superiority. Underlying this decision was the belief that the lottery would reduce the time and expense required to select licensees.

What perhaps was not anticipated was the birth of an entirely new industry of cellular application preparation services. These firms offer to provide consumers with the engineering, legal, demographic and financial planning expertise necessary to complete the comprehensive and detailed application required to enter the lottery. Public interest in the lottery, fueled in part by the aggressive marketing efforts of this industry, has resulted in total estimated annual sales by preparation services that may have been as high as between $50 to $100 million.[1]

As with many other goods or services, both honest and dishonest sellers of application preparation services have promoted the lottery to consumers. In 1985, the Federal Trade Commission successfully brought 2 federal district court cases against firms engaged in the nationwide sale of application preparation services through fraudulent representations. We do not claim to have eliminated all fraudulent representations in connection with the lottery. Instead, we are continuing to examine the practices of firms currently engaged in the sale of application preparation services, and we monitoring the compliance of those firms and individuals under court orders we have obtained.

Today, I will describe the fraudulent practices of the dishonest firms selling application preparation services based on what we have learned from the cases we have brought, the nature of the Commission's authority to proceed against them and the actions we have taken and are taking to reduce this problem.

APPLICATION PREPARATION SERVICES

Virtually anyone can offer to provide application preparation services. Once an application for a particular license has been prepared or obtained by a firm offering these services, the firm need only photocopy the original and insert its customers' names in the appropriate blanks to "prepare" additional applications for that same license.[2] In addition to those firms specifically created to prepare applications, other individuals and entities offering similar services include law firms, engineering companies, telecommunications consultants and financial planners.

Firms using fraudulent representations frequently use telemarketing—telephone rooms—to pitch their services. In addition, in television, newspaper and radio advertisements, these firms promote participation in the lottery as a "once-in-a-lifetime opportunity" to acquire substantial wealth. For what is described as minimal investment, these scam promoters virtually guarantee that their customers will win a license and become "very, very rich." For more details, consumers are instructed to call a toll-free number.

Those who call are subsequently bombarded with voluminous printed materials. The materials usually include slick brochures describing the company and the lottery process, maps of the markets for which licenses are available and detailed charts and graphs containing huge profit projections. Repeated telephone calls from salesmen invariably follow in which an oral sales presentation is made from a prepared script. If a sale is not consummated over the telephone, consumers are often invited to visit the firm's offices or to attend a seminar sponsored by the firm. Whether the sales pitch is given over the telephone, in a seminar or during an office visit, the script rarely varies.

To establish their credibility, scam promoters falsely describe themselves as "licensed preparers" or as "the only certified group preparing applications." Consumers are sometimes falsely assured that the firm has an insurance policy guaranteeing that the applications will contain all of the legal, financial, demographic and engineering data necessary to satisfy the lottery requirements. Scam promoter further promise that their customers will have no difficulty acquiring the multimillion dollar financing necessary to build a cellular system after winning a license through the lottery.

---

[1] This figure is a conservative estimate based on information about application preparation services acquired by FTC staff in the course of its investigations.

[2] Both the original and the mass produced copy are acceptable for entry into the lottery.

Once the prospective customer's initial suspicious have been allayed by representations about the firm's expertise, the salesmen begin the assault on the investor's dollar. To induce consumers to spend thousands of dollars to enter a lottery, the scam promoters make fraudulent representations, including misrepresentations about the virtual certainty of obtaining a cellular license through the lottery, misrepresentations about the enormous value of owning any license, and misrepresentations about the high profitability of operating any cellular system. The picture painted by the sales pitch is a rosy one, leaving consumers with expectations of large, immediate profits with little or no risk. These expectations are unwarranted.[3]

Application preparation services offer a wide range of programs designed to make their services affordable to most consumers. For example, one company we sued in 1985 promised to file an application for a customer for each of the 30 then available licenses for $150,000 cash. For as little as $2,500 cash and a $5,000 promissory note, the same company offered to sell a quarter interest in just one application.

The sales pitches invariably employ high pressure sales techniques. Salesmen frequently tell consumers that they must act quickly to purchase an application because the Federal Communications Commission will stop accepting applications in a few days, next week, or by the end of the month. Scam promoters have made these representations in the past even though the Federal Communications Commission had not yet announced the date when it would accept applications for the next available group of licenses, an announcement that precedes the filing date by at least two months.

The telephone room salesmen exert even further pressure on consumers to purchase their services as soon as possible by falsely representing that the company will file only a limited number of applications for each market. Should consumers request additional time to make a decision or to consult with their spouses or accountants, the salesmen attempt to embarrass or shame them into making immediate decisions on their own.

Victims represent a cross-section of Americans. They include prison guards, doctors, those in the military service, engineers, widows with young children and retirees looking for ways to augment their retirement income. Those without the necessary funds available are encouraged to liquidate their other assets to purchase cellular license applications. In one case, a disabled unemployed truck driver convinced his wife to mortgage her home to purchase two applications for $10,000 from one such company.

Consumers who purchase applications from scam promoters can expect to receive additional unsolicited telephone calls from the firm's salesmen. Former customers are encouraged to make additional purchases through continued fraudulent representations. Should customers ask whether the lottery has been held on the date represented by their salesmen, they are told that the Federal Communications Commission has delayed the lottery because of a "bureaucratic problem," a need "to clarify certain procedures" or because it is "behind in processing applications." Consumers who request refunds are sometimes told that the funds have already been spent for marketing purposes. Not surprisingly, few ever receive refunds.

THE COMMISSION'S RESPONSE

The Commission is most concerned about the nationwide sales activities of the application preparation services engaged in the kind of hard core fraud I have just described. The Commission's principal weapon against such fraud is a civil action filed in federal court under Section 13(b) of the Federal Trade Commission Act, 15 U.S.C. § 53(b), for violations of Section 5(a) of the Act.[4] Section 13(b) enables us to stop scams before they can inflict further harm on consumers and permits us to capture the scam's assets for possible redress to victims of the fraud.

Within the last five years, the Commission has acquired a good deal of experience investigating and bringing law enforcement actions against scams of this nature. In

---

[3] In fact, no firm can guarantee that its customers will win a license. Approximately 500 applications were filed for each of the licenses most recently awarded by the Federal Communications Commission. Thus, the odds of winning the lottery were 1:500. While joining in an alliance with other applicants previously permitted an applicant to improve his or her odds of winning at least a small share of a license, a proposal before the Federal Communications Commission would prohibit such alliance agreements in the future. Furthermore, according to the cellular licenses yet to be awarded is highly speculative, and it is unlikely that many of them will be marketable. The primary reason is that many of the remaining licenses, which cover rural areas of the country, are not expected to break even for twelve or more years and the long road to profitability makes them unattractive investments.

[4] Section 5(a) prohibits unfair or deceptive acts or practices.

the past few years, for example, we have investigated and shut down similar telemarketing scams involving the fraudulent sale of application preparation services for the Bureau of Land Management's lottery for oil and gas lease rights; [5] partnership shares in oil and drilling ventures; [6] silver and gold ore and ore processing; [7] rare coins; [8] oil leases; [9] diamonds and other precious gemstones; [10] and offers of "bargain" vacation packages in connection with the purchase of travel club memberships. [11]

In connection with the Federal Communications Commission's lottery, we have successfully brought federal district court cases against two of the largest firms engaged in the nationwide sale of application preparation services through fraudulent representations. [12] The two firms had aggregate sales of over 31 million dollars. The actions have put ten individuals and corporations under federal court order and have secured approximately one million dollars in redress for their victims. [13] More than 3,000 victims will be receiving redress checks in April or May of this year as a result of these actions.

In addition, Commission staff regularly monitors compliance with federal court orders that we obtain. Order violations are prosecuted as civil or criminal contempts of court, depending upon the seriousness of the violations. To date, three criminal convictions for contempt have been obtained by FTC staff against individuals involved in selling application preparation services for the Federal Communications Commission's lottery. [14] In addition, one criminal contempt matter is now on appeal.

Moreover, as we meet today, the Commission's staff is using our authority under Section 13(b) of the Federal Trade Commission Act to conduct nonpublic investigations of additional corporations and individuals offering cellular license application preparation services.

In addition to our own investigations, the Commission is working closely with state consumer protection officials and other federal agencies to coordinate investigations into the fraudulent sale of application preparation services and other telemarketing frauds. For example, at the federal level, the Commission is working closely with the Federal Communications Commission to investigate and prosecute such fraud. All public inquiries and complaints about application preparation services received by the Federal Communications Commission are routinely referred to staff at the Federal Trade Commission for review and response.

At the state level, in January of last year, the Commission announced the creation of a joint task force with the National Association of Attorneys General (NAAG) to combat telemarketing fraud more effectively through increased cooperation and information sharing. In the past, the Commission has found such cooperation to provide invaluable assistance to the successful prosecution of its cases. For example, in one case we brought against a nationwide seller of cellular license application preparation services, an investigator with the Arizona Attorney General's Office managed to infiltrate the telephone room operation of the defendant thereby providing us with rare insight into the operation of the company.

An important and recent development is the formation of the FTC-NAAG automated data bank in August of 1987 to enable the states and federal government to

---

[5] FTC v. U.S. Oil & Gas Corp., 748 F.2d 1431 (11th Cir. 1984); FTC v. Leland, 83-3589 CVM (Px), (C.D. Cal., filed June 2, 1983); FTC v. J&R Marketing, Civ. No. 83-1231 JE (S.D. Fla., filed May 18, 1983); FTC v. First Petroleum, Civ. No. 82-2744 EPS (S.D. Fla., filed Dec. 21, 1982).

[6] FTC v. Atlantex Associates, Ltd., Civ. No. 87-0045 (S.D. Fla., filed Jan. 12, 1987).

[7] FTC v. Volcano Mines, Civ. No. 86-0340 (D. R.I., filed June 4, 1986).

[8] FTC v. Security Rare Coin & Bullion Corp., Civ. No. 86-1067 (D. Minn., filed Dec. 30, 1986); FTC v. New England Rare Coin, Civ. No. 87-0330 WE (D. Mass., filed Feb. 11, 1987); FTC v. Rare Coin Galleries, 1986-2 (CCH) Tr. Cas. 67,388 (D. Mass. 1986); FTC v. Schoolhouse Coins, Civ. No. 87-05415 KN (Px), (C.D. Cal., filed August 19, 1987).

[9] FTC v. Alaska Land Leasing, Civ. No. 84-4516 AWT (Px), (C.D. Cal., filed July 23, 1984); FTC v. Trans Alaska, Civ. 84-2001 AWT (Px), C.D. Cal., filed March 27, 1984).

[10] FTC v. Kimberly International Gem Corp., Civ. No. 83-5268 JMI, (C.D. Cal., filed Aug. 15, 1983).

[11] FTC v. Amy Travel Service, Inc., Civ. No. 87-6776 (N.D. Ill., filed Aug. 4, 1987); FTC v. World Travel Vacation Brokers, Civ. No. 87-8449 (N.D. Ill., filed Sept. 28, 1987).

[12] FTC v. American National Cellular, Civ. No. 85-7375 WJR (Px) (C.D. Cal., filed Nov. 11, 1985); FTC v. The Cellular Corporation, Civ. No. 85-8231 WHO (N.D. Cal., filed Nov. 12, 1985).

[13] This figure represents funds in the possession of an FTC receiver. The Commission has received judgments for over $33 million in redress, but much of that amount is probably uncollectible.

[14] Two defendants pled guilty; the remaining defendant was convicted following trial. One defendant was convicted for violating asset freeze orders imposed by the court to preserve the defendant's assets for potential consumer redress. The remaining two were convicted for making misrepresentations to consumers in violation of court orders.

develop cases and prosecute fraudulent telemarketers more efficiently. The new FTC-NAAG automated data bank will give all users the immediate capability to learn whether an individual or corporation has been or is being prosecuted or investigated in another jurisdiction, and what evidence may be on hand in another jurisdiction. What once took weeks to learn will now take minutes.

Because scam artists often close up shop and flee, literally in the middle of the night, consumer redress is usually difficult to obtain. We hope that this data base will enable the Commission and the states to move more quickly to locate a scam's principals and their assets before they disappear. Of course, even when funds are not available for redress, formal law enforcement actions are important because well-drawn injunctions can force the worst actors out of the application preparation business and deter other bad actors from entering it.

CONCLUSION

In conclusion, the Commission shares the Subcommittee's concern about the problems engendered by the process used to award licenses to build and operate cellular telephone systems. Although the lottery has enabled ordinary citizens to own cellular licenses, many more consumers have been misled and defrauded by scam operators who have taken every advantage to abuse the lottery process. The Commission is continuing its work to put the worst actors out of business, and we are encouraged by the Subcommittee's efforts to join us in this battle.

Thank you for your interest in the Federal Trade Commission's activities in this area.

Senator INOUYE. Thank you very much.

Mr. Brock, you indicated that you do and you have rejected applicants who are considered to be speculators.

How many have you rejected?

Mr. BROCK. Let me ask Kevin Kelly, who is the Chief of our Mobile Services Division and has direct responsibility for that, to answer, if I may.

Mr. KELLY. Senator, in Markets 91 through 120, we extensively prescreened these applications and rejected hundreds of them. Beyond market 120, however, we changed the process so that we only carefully reviewed the winning application, and of those, we have rejected about 15 of the winners.

Senator INOUYE. And how do you determine whether one is a speculator or one is not a speculator?

Mr. KELLY. That is very difficult to do at the application stage when we are prescreening because the applications generally are well prepared. The points in the process where we actually determine whether or not there is speculation going on is in the petition to deny process and when the applications for transfer of control are received.

After we have a lottery, we announce the tentative selectee. At that time competing applicants and other interested parties have the opportunity to submit petitions to deny. We review those petitions to deny and the allegations of speculation at that time. If, after we award the construction permit or the license, the winning applicant is requesting transfer authority, we once again give the public a chance to comment on that, and we also review the speculation accusations.

Senator INOUYE. In order to qualify as a nonspeculator, what does an applicant have to have or do?

Mr. BROCK. We do not have specific criteria for that. Our rules require that the applicant be committed to serving the public at the time they apply for any license, including a cellular license. The question becomes whether there is any evidence that this

person had no intention of serving the public. If a challenger can make a credible case on that, the application may be denied. If not, there is a presumption that, because the applicant has stated that he intends to serve the public, that is a valid statement.

Senator INOUYE. What does the FCC do when it learns that soon after the granting of the application, the successful lottery winner goes out and seeks the highest bidder?

Mr. BROCK. Our rules provide that construction permits, which is the first stage of having won the application, may not be transferred freely. They may be transferred under certain cases, but if there is evidence that the recipient of a construction permit is merely seeking the highest bidder, we would deny that petition to transfer the license.

Senator INOUYE. On your time from application to service, I have here a summary on Market Nos. 241 to 305, that only 2 percent of the non-wireline lottery winners are now in service. When that percentage goes up, will the time lag not increase also?

Mr. BROCK. I do not believe so, Mr. Chairman. It is certainly correct that for the later markets there is a very small percentage now in service. These are ones for which construction permits were only granted during 1987, and therefore, in most cases these grantees have not had a chance to finish building the service. But we have not seen any pattern from early applicants to later applicants within a particular processing group.

Senator INOUYE. My last question, what is the filing fee?

Mr. BROCK. The filing fee is currently $200 per application.

Senator INOUYE. Mr. MacLeod, what are these firms charging? You said they exceed the filing fee.

Mr. MACLEOD. I think that the charges vary according to the number of applications bought. They would sell multiple applications, and according to the firm, but they could range from $600 and up. So there would be a markup of, say, 200 percent. The markup would cover the costs of the services plus the profits that these operators make.

Senator INOUYE. The committee will follow the procedure of calling upon Senators in the order of their arrival.

Senator Stevens.

Senator STEVENS. Mr. Chairman, I think my colleague is better prepared to ask questions than I, and so I will defer to Senator Packwood and ask my questions later.

Senator INOUYE. Senator Packwood.

Senator PACKWOOD. Mr. Brock, run me through the history of the awarding of the licenses initially.

You have some experimental awards in the 1970s in Chicago and maybe some other area. I am not sure. And then you started in 1981 full tilt. In most cases, if I read your testimony, the wired applicants were noncompetitive applications, is that correct?

Mr. BROCK. They were largely noncompetitive. We had some cases of a single applicant for wireline, some cases of a small number of multiple applicants. In most cases, the applicants, if more than one, settled among themselves to form a partnership.

There are a few cases where we have conducted a lottery on the wireline side as well, especially for the smaller markets.

Senator PACKWOOD. But in most situations you would have a dominant wired carrier and they would get the license almost as a gift.

Mr. BROCK. Yes, sir, that is correct.

Senator PACKWOOD. Okay. So now we have taken care of all the major—there are a few left to go, but the major areas, and the wired carrier has by and large gotten the franchises in most of those areas.

Mr. BROCK. Yes, Senator.

Senator PACKWOOD. All right.

Now, as I understand, what you want to do is to in some way limit the speculation, whether that be by a grant fee which you make reference to, or some other added cost, and yet not guarantee to the non-wired applicants sort of the same noncompetitive situation that the wired applicants had.

Do I read it right?

Mr. BROCK. Yes, sir, that is correct. We want to limit the speculation and get the service out to the public as quickly as possible. For the same reasons that we initially opened service to both wireline and non-wireline, we find it advantageous for there to be the possibility of new entry into these markets.

And I might add that, especially for the rural areas, many of these are very sparsely populated areas in which it is useful to have innovative kinds of services, and to permit new people who may not be the established carriers to have an opportunity to serve.

Senator PACKWOOD. Now, are the wired carriers in the metropolitan areas allowed to bid on the rural areas?

Mr. BROCK. A carrier with a wireline preference must have wireline telephone service within that area. A carrier—say a Bell Company—whose service area extended into the rural area would also be allowed to bid on that.

Senator PACKWOOD. Could Southern Bell bid on an area in the west where they do not have any wire at all?

Mr. BROCK. Southern Bell could not bid on that area as a wireline carrier. We would have no prohibition on them entering the non-wireline—I am sorry. Excuse me. I made a mistake there. They would not be allowed to.

Senator PACKWOOD. They are not allowed to bid, period.

Mr. BROCK. They are not allowed to bid outside of their own area.

Senator PACKWOOD. Now, here is what I am a little confused about. If they have the rural area wired, and I assume in 99 percent of the cases they do, in addition to the metropolitan area, in this case they are not going to be given a preference over the non-wired competitor. They will not be given the same preference advantage they had in the metropolitan areas.

Mr. BROCK. I am sorry, sir. In the rural areas there will also be the same dual structure of a wireline applicant and a non-wireline applicant so that the telephone companies will receive a service limited to telephone companies in the rural areas as well as the metroplitan areas.

Senator PACKWOOD. It seems to me the telephone companies have a whale of an advantage.

Am I mistaken?

Mr. BROCK. Yes, they definitely do have some advantage, sir.

Senator PACKWOOD. Some? It seems like a whale of an advantage to me. I mean, they are already in business and the wires run everyplace, and they can serve their entire area now, I assume.

Mr. BROCK. They can serve their entire area with ordinary wired telephone service. The reason I said some advantage rather than a huge advantage is that we have found in the later markets that the advantage in time of the telephone companies actually getting service up is relatively small compared to the non-wireline. The advantage is that the telephone companies have it without winning the lottery or trying to buy out another applicant.

Senator PACKWOOD. Let me switch very quickly to a slightly different subject.

We hear, many times, the telephone companies are criticized and people do not want to give them more power. Here I am talking about the RBOCs that were spun off from AT&T, because they have the block, they have the throat. You cannot get into an area except through their communications system.

Has there been any complaint from non-wired carriers about access to the wire to carry the message?

Mr. BROCK. There have been those complaints. We have taken a very strict position that they must give access.

Senator PACKWOOD. No, I understand that, and I realize the law requires it.

Mr. BROCK. Yes, there have been complaints.

Senator PACKWOOD. There have been some complaints even despite the fact they are supposed to do it.

Mr. BROCK. We have dealt with that matter. Yes.

Senator PACKWOOD. Now, run by me once more how you think we can reasonably come to a conclusion whereby you can eliminate the speculators, and I know the FTC is going to try to eliminate the fraud, without giving the non-wired competitors some kind of a disproportionate advantage in the application process.

I am not quite sure how you get from A to Z.

Mr. BROCK. Right.

It is a difficult problem, and that is why we have made a number of variations in our rules as we have gone through this process and are proposing additional changes at this point.

We believe that by having a fairly strict financial qualification standard and by then also reviewing requests for transfer, we can eliminate the pure speculation. Also, the elimination of the alliances is a significant step because that is one of the methods that has been used to promote the fraud, that a promoter——

Senator PACKWOOD. The elimination of the alliances?

Mr. BROCK. Yes. An alliance is a situation where a promoter will say, "I will provide applications for a large number of people. You will all go into the lottery, and then you agree that if you win the lottery, you get 51 percent and everybody else gets a small percentage. If you lose, you get a small percentage." And the promoter then claims this means you will at least get your application fee back.

Now, that obviously tends to promote speculation. If a person has to simply file an application and be fully responsible, the only way he can benefit from that is to provide service or convince us that

he has a good reason to transfer it. Then you begin to reduce that kind of speculation.

Senator PACKWOOD. Thank you, Mr. Chairman.

Senator INOUYE. Thank you very much.

There is a roll call at this moment, but I will now recognize Senator Adams.

OPENING STATEMENT BY SENATOR ADAMS

Senator ADAMS. Thank you, Mr. Chairman.

I want to first thank the Chair, my good friend, Senator Inouye, along with other members of this subcommittee, including my friends on the minority side for coming together and holding this hearing. Not being a member of this body, let me also thank the members for the opportunity to participate in what I believe will be some important eductional discussions.

Turning to the context of the deliberations, it is quite apparent that all of us sitting up here do agree on one basic premise. And that is that something has gone wrong with our non-wireline cellular license selection process. Let me provide you with some staggering figures: 97,000 lottery applications were received for 305 Metropolitan Service Area markets. It is estimated that up to 200,000 applications may be received for the soon to be selected 423 Rural Service Area markets. Additionally, we have the FTC now busier then ever processing fraud claims and settling out of court cases.

Logic tells us that something has gone awry. It is time for all parties interested in providing quality service to come together at the table and resolve this matter for the benefit of the real party in interest, the consumer.

Last December, with the help and cooperation of the Chair of this subcommittee, Senator Inouye, members of the minority, including Senator Danforth, and the Chair of the Commerce Committee, Senator Hollings, a brief moratorium was established to delay the institutiion of the RSA licensing process, allowing Congress time to review the issue. I am hopeful a resolution will be worked out before February 22, 1988, the date the FCC begins official notification of the RSA lottery process.

This hearing today will be an educational process. Cellular communications is a new and emerging industry with many competing interests. I expect this hearing to not only define the parameters of the issue, but begin moving us down a path toward a general framework of mutual understanding.

I would ask each of you testifying here this morning to work with us in a constructive and cooperative manner, allowing us the opportunity to find some middle ground where all of us can agree. Thank you.

You have asked most of the questions that I would have asked, and Senator Packwood has. I want to thank you for allowing me to participate in this. It seems to me that the process has gone awry, and I hope this hearing this morning will be an educational process and that suggestions will be made for a consensus.

I share the concern that Senator Packwood has that we have a monopoly already in the field, and this other group is now filled with both speculation and with fraud attempts. So I hope there will

be suggestions this morning, and that the groups that want to provide quality service will do it because otherwise our rural areas are going to be left with nonquality service and with great delays.

I would say, Senator Packwood, that when the applications go from some 15 per market to 97,000 and they expect 200,000 this time, that something is wrong in this, and I am hopeful this morning that we will get some suggestions as to how we might correct it and still maintain getting people into the market so it is not a monopoly.

Thank you, Mr. Chairman.

Senator INOUYE. Senator Stevens.

Senator STEVENS. Let me ask, Mr. Chairman, and I apologize for my voice. It is starting to go a little bit.

Mr. Brock, why is it that there are so many people who believe they have something to sell even after the successful applicant is selected?

I am told in one instance that several of the applicants got paid in excess of $1 million not to file suit to contest the award.

Are you aware of that?

Mr. KELLY. Yes, Senator, we are, and to be perfectly frank about it, there is not very much we can do about it. The numbers that I have heard were not as high as the numbers that you quoted, but they certainly were substantial amounts of monies. We have been told informally that a substantial amount of money has been paid to losing applicants to not file petitions to deny against the winner.

The reason for that is that if a person wins and he is anxious to go forward and build the system, he is delayed by a petition to deny which brings us into the process.

Senator STEVENS. Well, I understand that, but what leads them to believe that the petitions to deny would be successful? Have you knocked out some applicants with such petitions?

Mr. KELLY. Yes, we have, but not that many. It is not a question of whether or not the petition to deny is successful. The fact is there are certain costs that are associated with litigating the petition to deny, and there are time costs. It delays service to the public, and the winning applicant has to make a choice whether or not it makes more sense to simply pay off the would-be petitioner or fight through the petition to deny process.

Senator STEVENS. Well, I am concerned because a state like mine, where capital is very short and the economy is very bad, people that want to proceed are going to face these what I call strike costs if they are successful, and the ones who would have the best capability of proceeding with this new service might not be able to afford those strike costs, and therefore are not getting in. The people who are getting into this are the people who are speculators, who after they have paid off those strike claims, turn around and sell it to someone else anyway.

It reminds me of the BLM lottery on leases. For years we had a problem there. We finally solved that, and the way we solved it was a preliminary determination of eligibility, and only those who were eligible were in the lottery, and once you drew the successful lessee there was no challenge.

Now, why have you not done that?

Mr. BROCK. We did use a method fairly similar to that in Markets 91 through 120 where we did an extensive review of their qualifications prior to the drawing. We found that that was a very time consuming process, and felt that it was better to concentrate our resources on only those who were the winners.

I might say on your question, we certainly do not encourage the payoffs that you refer to, though that is the kind of question that many corporations face when sued by anyone. The question is, do they accept a settlement or do they fight it through litigation? In a law context, it is difficult to avoid that kind of tradeoff.

Senator STEVENS. Well, I was interested in what my good friend from Arizona said. He indicated he thought there ought to be something done so that we would have the individuals, particularly in rural America, who had some interest in the area and some background of business in the area, not necessarily this business, but some background, some proof of stability in the area, and at the very least that ought to be a condition, do you not think? Or are we to wait for people to come in from all over the country in Alaska, make an application to serve an area that they do not even know how to pronounce the names of the areas in rural Alaska, and there are plenty of people out there that have staked their lives there, they have put their money in there, and they want to be involved in this. They cannot possibly pay off these strike claims.

Someone getting in, looking at it as an investment, will put up the money, hire someone to make the application, file, and if he is successful, knows he is going to get paid by someone if he just has his application in, as I understand it, if he is qualified and if willing to say "I will present an application to deny this applicant his rights unless I get some money." That is blackmail.

Now, why should your agency be pursuing a policy which encourages blackmail from those people who have the ability and the know-how in the area?

Mr. BROCK. Well, Senator, we certainly do not encourage those kinds of payoffs or that kind of policy, but——

Senator STEVENS. I agree with that, and I am not accusing you of that, but the procedures you are following foster it. They foster it.

I am losing my voice badly, and I apologize. I do not want to sound like I am really shouting. I have got some of those, they did not work. The Alaska habit is to gargle with a little bit of whiskey, but then you get so you drink it, and I do not want to start that in the morning.

Why should you foster that kind of a policy? Why can you not have some sort of a screening or at least certification? What about if you have to have five business peers in the area say this person has ability, he has bank accounts, he has demonstrated his capability to manage? Why can we not have something that says, you know, these people are capable in the area?

Mr. BROCK. It would be possible to have any number of additional qualifications. Your suggestion is that perhaps we not allow petitions to deny. I think we would have a difficult legal problem on that.

We have a routine situation where all applications go on public notice. People have a right to comment on them and to challenge whether the applicants were legally qualified.

Senator STEVENS. I will tell you how you can deny those awfully fast, get rid of those. And that is to require a bond that is so substantial you are not going to present it unless you are really sincere.

These strike claims would be knocked out by the bond.

My time has expired. I would just ask one last question, Mr. Chairman, and that is for Mr. MacLeod. Why have you all not got into this somehow? The consumer is hurt when these applicants have to buy off these unsuccessful petitioners who are just blackmailing.

The amount of money that goes out to those strike claimants ought to be going into these new systems. Why have you not gotten into that?

Mr. MACLEOD. That is something that would be very difficult for the Commission to address, because what we are seeing are companies attempting to vindicate what they believe are their legitimate rights under the law.

Senator STEVENS. They are not companies. They are people who paid someone to file an application for them. They have never had anything to do with the telephone business. They are not even in it to run the telephone system.

They would not pursue it if they were successful themselves. They filed for the purpose of becoming strike claimants and they are getting paid off, and I think we can prove that.

Now, it seem to me that is an FTC question, too, and this money ought not to be going out the back door to these claimants. It ought to be going into establishing cellular systems out there in rural Alaska and rural Arizona and rural New Mexico and rural Kentucky and the places where we really need this service.

I do not want to get too personal. My wife's family has a ranch in Arizona that is beyond the telephone line. They cannot get telephone service. It is going to come in with this system.

And the Senator from Arizona is very interested. I know he is as interested as I am in the extension of this service, because it is going to be more costly to put lines in the areas we come from than it will be to put the cellular service in. I am sure you know that, Mr. Brock.

Mr. BROCK. Yes, it is certainly true that in many cases it is more expensive to put lines. We have recently established a specific radiotelephone service known as BETRS for that particular situation, though it is possible that cellular will be used as well.

Senator STEVENS. Cellular will be less expensive because you can still use it when you are in the city. I mean, it has an advantage to people in those rural areas.

I just think you have got to change the system somehow so the money that is available for the expansion of this service into rural areas goes into the service and not into the pockets of speculators and people who are really blackmailers as far as I am concerned.

I hope you really study this.

Mr. BROCK. We certainly agree, Senator.

Senator STEVENS. Thank you.

Senator INOUYE. Thank you very much.

I am certain all of us on this committee are concerned with the interest of the consumer. That is primary. We have been told that the financial windfalls are huge. I would assume that you have monitored all of your applications. How do they range in dollars?

Mr. BROCK. Do you mean the kinds of prices that people pay for applications?

Senator INOUYE. That is right.

Mr. BROCK. Let me distinguish two different cases. Once a system is built and it is functioning, then, although we approve the license transfer, we do not restrict the ability of people to transfer those or check the prices. In cases where a person asks to transfer interest in an unbuilt system, we then do monitor some of the conditions of the sale.

We do not have a good record of the prices people have paid. We do know that these are very valuable systems and go for substantial amounts.

Senator INOUYE. What do you mean by "valuable and substantial"? You must have some numbers.

Mr. BROCK. Yes, we do. What we see reported in the trade press and have no reason to disbelieve is that systems are going for prices on the order of $10 to $20 per person in the population area. For a city of a two hundred thousand population, a system would have a value of approximately $2 million to $4 million.

Senator INOUYE. Do you make any distinction between any rural area or do you treat all rural areas alike? And I am coming to a situation such as Alaska and Hawaii, where you have communities that are physically separated by a wide expanse, in the case of Alaska of land, in the case of Hawaii by water.

It is not the typical metropolitan area and adjacent to that a rural area. Should any distinction be made?

Mr. BROCK. We do not presently make a distinction for those kinds of areas. We have divided the country into 425 rural areas and there is no substantial distinction among them in terms of how we would allocate the licenses.

Senator INOUYE. How do you treat a state like Alaska? I am just curious.

Mr. KELLY. I cannot exactly remember the counties in Alaska that are in the RSA's. I do not have the RSA list available to me.

What we did in Alaska I think is that we had one MSA in Alaska. We divided the remaining portions of the state into RSA's, which we will accept applications for separately.

Senator STEVENS. We do not have counties, Mr. Chairman.

Senator INOUYE. I have a map here. I suppose Anchorage is the MSA.

Mr. KELLY. Yes.

Senator INOUYE. And the rest of the state is RSA.

Mr. KELLY. That is correct.

Senator STEVENS. It looks small, but it is one-fifth the size of the United States. And any one of those things is as big as Massachusetts, and that is the problem. And people do not understand that when they file that application. They do not understand what they would be getting into if they were successful.

Do you hold them to performance? Suppose I made an application through one of these filing agencies and I win. What is the penalty if I do not perform within a certain period of time?

Mr. BROCK. Senator, our current rules require that an applicant have a system up and running 18 months after it is granted the initial construction permit. And if an applicant fails to do so, it would then forfeit its winning.

Senator STEVENS. The answer is no penalty; you just lose.

Mr. KELLY. Senator, in Alaska, just for the record, there are three RSA's. I can tell you what they consist of if you would like.

Senator STEVENS. Go ahead.

Mr. KELLY. Okay. Alaska 1 is called Wade-Hampton and it consists of Wade-Hampton, Nome, and—I will not pretend to be able to pronounce all of these.

Senator STEVENS. I want to see the size of it.

Mr. KELLY. Kobuk, North Slope, Yukon, Fairbanks, North Star, and Southeast Fairbanks. That is Alaska 1.

Alaska 2 is——

Senator STEVENS. That is an area one and a half times the size of Texas.

Mr. KELLY. Alaska 2 is Bethel, Dillingham, Bristol Bay, Kodiak Island, Kenai Peninsula, Matanuska, Valdez-Cordova, and the Aleutian Islands.

And Alaska 3——

Senator STEVENS. The Aleutian Islands go further west than his state. That is 2,400 miles you just talked about. Now, that is the problem, you see. That is the real problem.

It is not possible for someone to come into that area and deliver cellular services unless they really know what they are doing. You should not allow anyone to apply for that unless they really know what they are doing.

I think there ought to be a penalty for nonperformance. That would be an interesting thing, Mr. Chairman, a penalty for nonperformance, and make them nontransferable. Then you would lose this problem.

They are transferable. As long as they are transferable, you can either sell them or you can get paid off if you are not successful in the drawing.

I am sorry, Mr. Chairman, sorry to interrupt.

Senator INOUYE. I would like to advise the panel that the Senators who are not in attendance today have many questions they would like to submit for your consideration and response.

With that I would like to thank you for helping us this morning, and this committee will stand in recess for ten minutes.

[Recess.]

Senator INOUYE. We will now call upon our second panel, consisting of: Mr. H. Robert Neff, President, Cellular of Northwest Ohio, the owner and operator of a non-wireline cellular system in Billings, Montana; Mr. John E. McCaw, Executive Vice President, McCaw Communications Companies, owner of several cellular licenses in metropolitan areas; Mr. E. William Henry, Esquire, attorney for the U.S. Independent Cellular Telephone Association, a group representing applicants in the rural lotteries; and Mr. Steven S. Seltzer, President, Modern Communications Corporation,

a radio common carrier providing an older form of mobile telephone service.

Gentlemen, welcome. And I will now call upon Mr. Neff.

STATEMENT OF H. ROBERT NEFF, PRESIDENT, CELLULAR OF NORTHWEST OHIO

Mr. NEFF. Mr. Chairman, members of the committee.

Thank you for the opportunity to be here. You are looking at a so-called speculator in cellular markets. I have applied for licenses and won a majority interest in Billings, Montana, and other minority interests which I still retain.

Thousands of others who won cellular ownership through settlement groups are today assisting in building those systems. If this represents speculation, would all of us have been called speculators if we had merely bought McCaw stock?

I built my system in about 120 days. It was on the air before the wireline. In terms of population, Billings is smaller than at least half of the rural cellular markets. This is proof that the RSA's can be built by independent entrepreneurs.

I am not unusual. There are dozens like me who have built markets won in lotteries. I have resisted offers to buy my system that would have made me an instant millionaire.

I personally would benefit by any proposal to award RSA's to MSA winners. But there is no reason to stop me or any of the thousands of other qualified citizens like me from applying in the RSA's.

Now, companies like McCaw might say that all of us who won cellular lotteries put enormous price tags on our cellular permits and sold them to the highest bidder. This is simply not true. The truth is that almost one company, McCaw, paid enormous prices to buy many of these markets. Why? Because it was making the public offering.

McCaw received from the public more than double the amount that it paid for these markets. It now has over 100 markets.

None of the people that filed lotteries had any idea that McCaw or anyone else would try to corner the market on cellular systems. Yes, permits change hands and some profited. But it is the speculation of the big companies that fueled any buying frenzy, and not the other way around.

Many of these sales took place shortly before the companies launched their effort to restrict the eligibility requirements. If speculation did occur, the old adage applies. Like it takes two to tango, it takes two to speculate.

But the important question here today is who should Congress entrust to build the RSA's? You can entrust qualified, independent applicants that include cable operators, broadcasters, publishers, and a variety of business people, or you can have a closed system of awarding the RSA's to already entrenched interests.

But the big players are here today and gone tomorrow sometimes. Metromedia was the largest cellular company until it sold all of its holdings. MCI sold its cellular holdings for hundreds of millions. Bell South is buying MCCA out.

It seems the only difference between the big companies that buy and sell and the little guys who do the same thing is the scale on which they do it. Sell one market and you are a speculator, but consolidate markets and sell them and you are an astute businessman. Sell all of your markets and get out of the business and you are a financial genius.

Awarding the RSA's to MSA winners will help to create monopolies, particularly regional ones. Will Congress then have to pass legislation to break up these monopolies?

Giving RSA markets to MSA winners will likely result in skimming. They would build more profitable MSA's first and delay the service to the public in rural areas, just as cable and phone companies did.

Closed entry will be a Congressional endorsement of a small few companies that own one-third or more and a few other large companies, without any guarantee that they will build, and with a total disregard for their track record.

What guarantees does Congress have that it will not change businesses? Further, MSA operators will not necessarily build the RSA's faster. A good example is Melbourne, Florida, where McCaw Communications Company obtained an option in March of 1986. To my knowledge, it has not broken ground on a single cell site there.

Is this speedy service to the public? The point is, I can build an RSA just as quickly and efficiently as any adjacent MSA owner.

For these reasons, I urge Congress to maintain open entry. The big cellular companies want to restrict entry and thereby stop thousands of entrepreneurs like myself from at least having the opportunity to take the risk, to add value and provide service to the public. They want it all and they want Congress to give it to them, almost free of charge.

Such a Federal giveaway is not consistent with the competitive communications policy this Congress has fostered. It is unprecedented, unwarranted, and in my opinion un-American.

Thank you.

[The statement follows:]

STATEMENT OF H. ROBERT NEFF II

Thank you for the opportunity to appear before you to address issues which I believe are critical to the development of a competitive marketplace for rural cellular telephone service. I am testifying today as the lottery winner and cellular operator of the Billings, Montana cellular system and as a member of the Cellular Association of America, Inc.

I first found out about cellular while working as a deep sea diver around Malaysia and Singapore. I became very interested in cellular and could not believe we did not have it in the U.S. When I returned, I joined partnerships which applied for cellular licenses in top-90 MSA markets. In these top-90 markets, there were full market settlements.

In markets 121-305 I filed applications and won small ownership positions through settlement groups and am today making capital calls to assist in building those cellular systems. Additionally, on November 21, 1986 I was fortunate enough to be selected as the non-wireline permittee in Billings, Montana. After reviewing my qualifications post-lottery, on August 17, 1987, the FCC awarded my company the permit for the Billings MSA. I am the President of Billings Cellular Telephone Company (BCTC). The Billings MSA ranks in the bottom 15% of the metropolitan statistical areas ("MSAs") and it has a lower population density than the average rural cellular service area ("RSA").

Because timing was critical, in order to get service to the public I immediately proceeded to build the system. The system was built and I began testing it with about 50 subscribers, only about four months after I was awarded the permit. Mine was the first system built in my area. I constructed ahead of the wireline, which is still not in operation. I also constructed well ahead of McCaw Communications, which holds the construction permit in nearby Spokane, Washington.

I mention these facts not to blow my own horn, but because they attest to the critical issue before this Committee: The capability of applicants to bring quality cellular service to the public. This is not something that can be generalized from how big a company is, or how many dollars are in the corporate coffers, or where a company is located. It is not even necessarily a function of experience. It is, rather, a function of a particular applicant's individual qualifications, and that is why I am here today — to tell this body that limiting rural cellular eligibility to a few big companies would be a regrettable mistake for the public. Rural area service will be initiated faster and more efficiently and at a lower cost to the public, if the government encourages the participation of many independent businessmen and women, rather than depend on a few companies who were lucky enough to win an earlier lottery, or those companies who launched public offerings by buying up earlier markets. For the following reasons, I support, without equivocation, open entry into the FCC's rural cellular lotteries.

Should Congress adopt an approach to the rural cellular markets such as that proposed in the Report accompanying H.R. 2961, which would limit rural cellular service area ("RSA") applications to those companies operating adjacent metropolitan service area ("MSA") cellular systems (or operating two-way RCCs in the rural area), I would benefit personally because I am a cellular licensee and there are rural markets adjacent to Billings. I suppose, therefore, that I should be in favor of the proposal to restrict, in part, future eligibility for the rural markets to adjacent licensees. But I am not. I believe that concentrating control and consigning the future of rural cellular service into the hands of a few lucky companies is economically inefficient, fundamentally unfair, and could do a tremendous disservice to millions of rural Americans. If the changes proposed by the House Report had been in place earlier, I would never have been allowed to apply for the Billings, MT license, and Billings, MT would likely still be without cellular service. If this bill is put through, I will be prevented from applying for rural cellular licenses even in my own home town area, for which I put applications together in 1983 in anticipation of the filing date of December 10, 1983 which was set forth in then-existing FCC Rules.

A few cellular companies have launched a kind of negative advertising campaign in order to convince Congress to limit eligibility in the RSAs to themselves. They argue that open entry has resulted in the selling of newly-built systems and unbuilt cellular permits by the small, independent lottery winners who the companies claim are nothing but "speculators" in FCC cellular authorizations. Such a characterization is not only untrue, but an insult to all those independent business persons like myself who have made a valuable contribution to the cellular industry.

First, many smaller, independent selectees have, like me, built their systems. I know some of them personally because we share common goals and interests. For example, Ken Iscol has built Amarillo, Texas; Archie Kendrick - South Bend, Indiana; and Billy Parrott - Roanoke, Virginia. Norma Rae is in the process of building Wilmington, North Carolina; Charles Fitzgerald, Jacksonville, North Carolina; Natubhai Patel - Santa Cruz, California; Brian O'Neill - Panama City, Florida; Celutel, Inc. - Charleston, West Virginia and Modesto, California; Richard Bawab - Victoria, Texas; and Ed Forks - Montgomery, Alabama. The chart attached as Appendix I shows the multitude of metropolitan cellular systems that have been built or are being built by small, independent operators like myself, and it illustrates the opportunities that have been provided to minority business people to get into this business.

82-856 0 - 88 - 2

Secondly, as some of the cellular companies tell the story, it sounds like all of the independents who won cellular lotteries immediately hung out enormous price tags on their cellular permits and sold to the highest bidder. That is simply untrue.

Companies like McCaw almost single handedly created the marketplace for cellular permits in two ways. First they refused to cooperate with the little guys who wanted to build. I have been told of instances where independents who won small markets adjacent to large cities were warned by the major market operator that they might as well sell and get out because they could expect no technical support from the major city systems. And, when faced with such a choice, of course, some of the little guys sold.

Next, most of the large companies planned to have public stock offerings and McCaw did have such an offering last fall. How was its stock priced? It was priced largely based on the number of potential cellular subscribers the company controlled in its franchise areas. Well the company was not lucky enough to win an inordinate number of lotteries so it had to buy franchise areas from existing cellular permittees. A private company wishing to go public pumped up the potential cellular customers it controlled by offering inflated, some might say even outrageous, prices to buy cellular construction permits and operating systems. The value to the company of the increased potential cellular pops on the prospectus was worth two to three times the price the company actually paid for the pops.

When viewed in this perspective, it is clear that not all small, independents sold their permits, and even those who sold were not necessarily speculators. Yes, many construction permits changed hands and some small independents profited - but it's the speculation of the big companies that fueled any buying frenzy, not the other way around.

A few large companies have almost single-handedly bid up the price for unbuilt MSA systems to four or five times the prices prevailing when the MSA applications were filed. Some of these transactions took place in the past sixty to ninety days when these companies knew that they would be launching an effort to restrict eligibility. Selling under such circumstances is neither trafficking nor speculation.

Look at another big company, Metromedia. For a year, it was the largest non-wireline cellular telephone company until it sold its holdings - most of which were won in comparative hearings and sold soon after construction. McCaw Communications used to be a major cable television company until it decided to exit from that business. What assurance do we have that, seeing the right opportunity, it will not exit from the cellular telephone business? MCI sold its cellular holdings, most of which were unbuilt or newly built, for hundreds of millions. In yesterday's Wall Street Journal it was reported that

Bell South is buying MCCA. The turnover of large companies in cellular has been substantial. It seems that the only difference between the Metromedias and McCaws and MCCAs who buy and sell construction permits and the little guys who do the same, is the scale on which they buy and sell. Sell one market and you're a speculator. But consolidate five or ten markets and sell them as a group and you're an astute businessman? Sell all your markets and get out of the business like Metromedia and you're a financial genius.

Frankly, a certain amount of buying and selling in the cellular industry is necessary, and even healthy. The situation for abuse of the RSA permits does not exist because the large companies no longer have incentives to purchase permits at inflated prices and in fact may not be interested in many of the RSAs. Certainly, if Congress gives RSAs away, the big companies will take them (and some companies desperately need this Congressional subsidy.) But the economics are not there for the wide-scale coercive purchases that occurred in the MSAs. I believe the so-called "trafficking" problem, if any, is self-correcting and will cease without Congressional intervention.

For the RSA winners, flexibility in deciding to build, operate or sell is necessary. Certain RSAs may lend themselves consolidation with other RSAs to form one regional rural system. Operators may want to cooperate or joint venture with adjacent markets, and expansive single-operator systems may be most economical in certain areas. Thus, restrictions on the transferability of RSA permits threaten to harm rather than help RSA cellular developments, regardless of whether the permits are owned by small independents or the few big companies that dominate the business.

On the operational side, a variety of technical reasons also argue vehemently against any federal government give away of these valuable RSAs to a few large companies such as McCaw, which controls almost one-third of all the MSAs by itself.

Foremost, the majority of the area in an RSA is virgin territority as far as cellular service is concerned. An MSA operator will likely "cream-skim" and serve only a small part of the RSA, leaving most of the RSA without cellular service for quite some time. An independent RSA operator will be economically motivated to serve more of the RSA, including truly "rural" areas where cellular can be used to deliver basic fixed telephone service. Unlike the MSA operator, an independent RSA operator can only be successful in small, rural areas by maximizing service to his entire franchise area.

There are many off-setting economies that could be generated by a stand-alone RSA system. Back-hauling voice messages all the way to the MSA operator's switch can involve large capital outlays as well as recurring expenses. You can be sure these costs

will be passed on to the customer. Existing MSA-located transmitting equipment is useless beyond MSA/RSA border areas. Small American-made switches and base station equipment such as that manufactured by Plexsys Corp. in Corinth, Mississippi are actually less expensive than the larger and more cumbersome switches.

Common ownership of MSAs and adjacent RSAs is not required to provide wide-area cellular service. Existing cellular technology and FCC regulations permits the interconnecting of separate cellular switches or the sharing of a switch by independently owned cellular systems. Such arrangements now are operating in the Cleveland/Akron/Canton MSAs and in the non-wireline systems of New York City and Northern New Jersey. Moreover, intersystem interswitch hand-off has been successfully done in certain Texas markets. And this is an area that could benefit from federal legislation to ensure that further interface refinements and are not stymied by uncompetitive actions and lack of cooperation among adjacent cellular operators.

Independent RSA licensees will focus their marketing and service efforts on their rural areas. A RSA authorization will be more important to an independent licensee as likely its sole FCC license than to a larger MSA operator who merely views it as a service area expension. (Many MSA licensees could likely warehouse the RSA authorization as long as possible using it only when most MSA expansion is completed.) Even with switch sharing or system interconnection; an independent RSA license should have both the ability and motivation to custom-tailor its service to the rural markets.

But the issue here is not really the buying and selling of permits. It is not big businesses versus the little guy, and it is not even whether a few speculators have made a profit. To quote the Report accompanying H.R. 2961, the issue the Committee is faced with is how best to achieve the Commission's goal of "rapid and efficient provision of cellular service to the public."

No matter what arguments some companies put forth to justify the whole scale annexation of the RSAs for the benefit of a few corporations, the issue boils down to this: does the system work? And I say, yes it does. I challenge any of these panelists or members of this Committee to point out a communications service which has gotten off the ground faster than cellular telephone service. FM radio and UHF languished for years before expanding. Television broadcasting has been around for over forty years and still some rural Americans cannot receive a full complement of TV signals. Low power TV was supposed to provide a solution early in this decade, but that service has yet to get off the ground. Cable television started in 1948 and still many areas, including this city of Washington, do not have cable available. Another example is multichannel multipoint distribution service (MMDS). To date, less than a handful of MMDS operators exist in the

entire United States despite the fact that MMDS has been around about the same length of time as cellular telephone.

The evidence that open entry has worked and is working is overwhelming. Over a million Americans use cellular telephone service today who had never heard about it just a few years ago. The FCC's process has helped to get, and keep, things moving. Under the existing system, runners-up in the FCC lottery system have acted as private attorneys general, helping to ensure that the winning selectee abides by all the FCC requirements and is qualified to build the system. Where it felt that problems existed in the application process, the Commission has investigated them and has referred alleged abuses to the Department of Justice. (And the FCC's recently instituted fee schedule will likely cure that abuse.) Cellular settlement groups have been permitted and have flourished thereby allowing small independent investors to obtain actual minority ownership in operating systems. The settlement groups have encouraged the pooling of talent and knowledge which has benefited the system operations. There is no reason to change the existing system because it appears to be operating efficiently. The FCC is geared up to process two applications or two thousand applications per market, and the Federal Government could certainly benefit from the projected 20 million in revenues that will be generated by open entry filing fees.

If on the other hand Congress proceeds to prohibit open entry and just enables the privileged few to apply for the licenses to serve rural markets, it will be creating procedural mayham with substantial delays while federal closed-entry rules are appealed in Court. Gross operating inefficiencies will develop not to mention the fostering of a monopoly that the government will probably have to break up in a few years. A windfall worth hundreds of millions of dollars will be given to a few big companies which the government is not assured have the finances or intention to build and operate rural systems. (Just look at McCaw's 10-Q SEC filing which states:

> The Company must continue to raise capital for the acquisition of additional cellular interests, the construction of unbuilt systems, the operation of systems and the servicing and refinancing of indebtedness. These additional capital requirements will be substantial and may be financed largely through the issuance of additional indebtedness. The Company may also sell additional equity. Although it is not currently anticipated, the Company could also raise additional capital by selling assets. There can be no assurance that the Company will be able to obtain such additional financing when needed, or if it is able to obtain such additional financing, that the terms will be favorable to the Company.)

Even if the company claims its financial strategy has changed, what is to prevent it from the asset sales contemplated in the 10-Q?

Multiple system operators will win a certain number of markets and these may, or may not, be the ones they would have chosen in an open marketplace. Because of this distortion in the marketplace and lack of competition for licenses, rural consumers could suffer. Existing cellular licensees are less likely to bring service rapidly to rural markets than individual entrepreneurs. In fact, their incentive will be the reverse. MSA operators will concentrate first on their MSA operations and then saturate the adjacent areas that can be reached with their existing equipment before investing anything to serve the truly rural markets which has been handed to them. Closed entry will in fact encourage the warehousing of unbuilt rural cellular authorizations. Look at what continues to happen in the cable television field where rural customers located within a franchise area are served last, if at all. Look at what is already happening in the cellular field. McCaw, for example, has yet to build Melbourne, Florida immediately adjoining its Orlando system, or Chattanooga, Sarasota, Bradenton, or Johnson City/Bristol. (The 3-year construction permits for Chattanooga and Bristol expire next week and McCaw will have to ask for an extension of time to build.) It just completed Tampa, a top-30 market. Appendix 2 lists all the markets McCaw has yet to build and the length of time it has had the construction permits in these markets. Further McCaw may be already financially overextended through previous commitments. Thus, there is no reason to believe it will build rural systems as fast as independents can.

Contrast this with the telephone experience in rural areas. Over a thousand independent telephone companies bring service to the nation's rural phone customers - customers the big city phone company would not serve because it was not economical to do so. A nationwide backbone of independent rural cellular operators should be permitted to bring the same kind of service to rural cellular customers.

For these reasons, I respectfully request that Congress maintain open entry into the FCC's rural cellular lotteries. The big established cellular companies seek to restrict entry and thereby deprive thousands of entrepreneurs like myself from having the opportunity to take the risk, add value and provide service to customers for only one reason: greed. They want it all and they want Congress to give it to them lock, stock and barrell, almost free of charge. Such a federal give away is not consistent with the kind of competitive communications policy this Congress has fostered. It is unprecedented, unwarranted and in my opinion, un-American.

Thank you.

I would be pleased to answer any questions.

Senator INOUYE. Our next speaker is Mr. John E. McCaw, the Executive Vice President of McCaw Communication Companies.
Mr. McCaw.

STATEMENT OF JOHN E. McCAW, JR., EXECUTIVE VICE PRESIDENT, McCAW COMMUNICATIONS

Mr. MCCAW. Thank you, Mr. Chairman.
Mr. Chairman, members of the subcommittee, I am John E. McCaw, Jr., Executive Vice President of McCaw Communications Companies. I would like to summarize my statement and submit my full written statement for the record.
Senator INOUYE. All of your statements will be made part of the record.
Mr. MCCAW. I am on the board and the legislative committees of both Telocator and CTIA, the two cellular industry trade associations. However, today I am speaking as a representative of McCaw Communications.
The subject of this hearing is the single biggest issue facing the cellular telecommunications industry today. I would like to address three major points.
We would like to see a public policy developed which provides efficient quality service to the rural consumer.
Number two, the problem of service to the rural consumer is being jeopardized by a flawed system which we witnessed as MSA licenses were granted.
And finally, there is a need to develop a new system that brings committed service providers to the table and at the same time ideally allows the qualified entrepreneur to participate.
Our goal in these hearings is to develop a public policy provides efficient quality systems to the rural consumer as expeditiously as possible. At the same time, we would like to provide the rural consumer with the full benefits of a procompetitive environment, between two economically viable competitors, to ensure that he has a true choice, and that he gets his service quickly at the least possible price.
In the interest of the rural consumer, our objective, should be to provide competition between the service providers rather than between the hundreds of thousands of applicants, few of whom could or would provide quality cellular service. The problem, in my view, is that we are trying to achieve these goals by using a system that has not worked. The FCC has tried very, very hard to come up with a method of allocating licenses which began with a comparative hearing process. These hearings were costly and very time consuming, and in many cases, could have created delays of up to 3–5 years for the non-wireline side.
After that occurred, the FCC went to a lottery system. The problem we experienced there was that as the cellular telecommunications industry began to mature inexperienced applicants were being granted licenses and were not able to compete against the Regional Bell Operating Companies.
Two things occurred. The people not being effective competitors prevented a clear choice for the consumer, and we have negated the cost economies of creating regional cellular operations.

In the RSAs this problem is even worse than the lower round MSAs because the RSAs are smaller in population by nature and more spread out, making the economics even worse in these areas. We come here today hopefully to come to some kind of solution whereby we can create quality efficient service to the rural consumer.

We are looking for a licensing process that would result in committed operators providing the service. In a perfect world we could have the entrepreneur at the table with companies like ours at the table, and I think there are ways that we all can cooperate I think it is very important, at a minimum, in the granting of these 425 RSAs, that in every case we have a committed, financially and technically qualified operator at the table.

There is precedent for this. The FCC in the past has used comparable limitations as far as eligibility is concerned to promote fast, efficient service. We are diligently pursuing an outline in the industry that would come up with a compromise whereby everyone can participate. I think it is very, very important that committed operators are there at the same time we as a company and we as entrepreneurs are concerned that the entrepreneurs are not precluded from this process.

There is one concept that has been discussed among the many players in the industry, and they are wide and varied, the concept has been referred to as a dual lottery. This lottery would be a combination of the eligibility restrictions that we proposed at the end of the last Congress, and the lottery system.

In summary, there would be an initial lottery, where one applicant would be selected in each one of the 423 markets. He would then join the other eligible applicants (eligible due to their adjacent cellular operations, or their conventional mobile telephone operation in the RSA) in an attempt to reach a settlement. If these applicants were unable to reach an agreement, a second lottery would be held among them. It has been our experience that these groups will reach a settlement in most cases.

We look forward to working with all interested parties in trying to reach agreement and provide service to the public quickly. Thank you again for this opportunity.

[The statement and questions and answers follow:]

STATEMENT OF JOHN E. MCCAW, JR., EXECUTIVE VICE PRESIDENT OF MCCAW CELLULAR COMMUNICATIONS, INC

Mr. Chairman and Members of the Subcommittee, I am John E. McCaw, Jr. I deeply appreciate the opportunity to appear today at these important hearings on rural cellular telecommunications policies.

I am particularly pleased to be here because my company, my family and I have dedicated substantial resources and energies to the realization of cellular technology's fullest possible potential. We have been active industry participants in virtually all aspects of cellular policy issues from the service's inception to the present. As a result, we have significant first hand experience with the practical, real world effects of the regulatory process upon the cellular industry and the provision of cellular services to the public.

McCaw has been involved in the communications industry since 1937. It first entered the radio industry and then diversified into television in the 1950s. In the mid-1970s, McCaw entered the fields of paging and conventional mobile services and, in the early 1980s, McCaw became an active participant in the new cellular industry. Today, McCaw has divested itself of most other lines of business in order to concentrate primarily on cellar telephone services. McCaw is committed to the expeditious

development of the cellular industry to facilitate the provision of rapid and efficient cellular services to the public. This commitment is evidenced by McCaw's construction and operation of more cellular systems than any other service provider.

At the outset, I want to emphasize the timely nature and critical importance of this Subcommittee's hearings. The single most important issue in the cellular telephone field today involves the establishment of application processing policies for Rural Service Areas ("RSAs"). If existing policies are maintained, the FCC can expect to receive over 200,000 applications for the 423 RSAs, all but a few of them for the non-wireline allocation. This flood of paper will have been stimulated by "application factories" offering applications for as little as $200 a market with promises of enormous financial rewards to lottery "ticket holders". Their promotional material typically urges "investors" to buy interests in sets of filings for all 423 markets—some even encourage husbands, wives and children to file independently. Indeed, the application factories' latest gimmick has been to solicit foreign participation in mass fillings by describing the process as a U.S. giveaway of lucrative licenses.

If action is not taken to prevent this flood of applications from speculators, several serious adverse consequences are inevitable:

Service to rural Americans will be delayed as the FCC struggles through the mountains of applications and ensuing litigation.

Cellular permits will be awarded to persons who have no real commitment to building systems and bringing service to the public.

Serious cellular service providers like McCaw who want to offer efficient systems integrating RSAs with adjoining MSAs will be denied the opportunity to bring high quality, competitively priced service to the public.

The public interest advantages to the Commission's competitive industry structure will be undercut because wirelines will have a substantial headstart and cost advantage over the non-wireline operators.

In sum, the RSA problem is serious and pressing.

During the last session of Congress, considerable attention was focused upon a plan designed to prevent these problems. The proposal would establish qualifications for applicants seeking FCC licenses for non-wireline cellular telephone systems in less densely populated RSAs. Under this proposal, RSA applicants would demonstrate their qualifications by showing themselves to be either common carriers holding cellular licenses in the larger adjoining Metropolitan Statistical Areas (MSAs) or two-way mobile carriers already providing certain levels of service in the RSA. This plan was designed to ensure that cellular systems in rural areas are built and operated in a timely manner by cellular operators who have undisputed qualifications and a proven commitment to the prompt provision of cellular service. In addition, the proposal would actually increase the level of competition in the cellular telephone industry by ensuring strong effective competitors to the Bell Operating Companies and other wireline cellular telephone operators. The proposal thus sought to promote competition *and* ensure the faster availability of cellular service to unserved rural Americans. As I will explain more fully below, McCaw believes that this basic approach would best serve the public interest for several reasons.

THE AMERICAN PUBLIC'S IMPORTANT STAKE IN CELLULAR RSA POLICIES

Since the inception of basic exchange telephone service in the United States, provision of service to rural areas has faced special economic and technical difficulties. The unique new capabilities of cellular technology have enormous potential for bringing rural Americans the benefits of modern telecommunications. For example, cellular is vastly superior to conventional mobile service, which uses only one powerful antenna and a few channels and thus is limited in the number of users and the service area.

Cellular, in contrast, is capable of serving many subscribers at once because it divides service areas into cells. A "cell" is two to ten miles across and contains an antenna connected to a low-power radio transmitter and receiver. A cellular user can move from cell to cell within a service area and his calls will be automatically transferred without interruption.

If mobile units are sufficiently separated, they can both use the same frequencies without suffering interference. Where several mobile units need service in the same cell at the same time, they can be accommodated by utilizing several frequencies in each cell.

The quality of transmission from cell to cell is assured by a "hand-off" procedure by which a central computer, called a mobile telephone switching office ("MTSO"), is alerted by a cell site that an in-progress call is operating at an unacceptable

signal level. The MTSO makes a determination of which adjacent cell site is closest to the mobile unit, signals both cell sites and the mobile unit and, in a matter of milliseconds, reroutes the call to the new cell site on a different channel with no perceptible interruption in service. This hand off procedure and frequency reuse are the hallmarks of cellular service. In comparison with conventional mobile service, these features greatly increase the number of possible subscribers and expand the service area. With these improvements, cellular telephone technology will be useful for many purposes to rural Americans.

The RSA licensing policies adopted by the FCC and the Congress will inevitably impact the costs, efficiency and quality of RSA cellular service availability. The RSA markets are often natural extensions of more populous adjacent MSA service areas. Often RSAs are bound together with a neighboring MSA in an economic and cultural community of interest. Accordingly, if existing MSA operators obtain RSA licenses, they can serve the RSA and the MSA with common cellular telephone switching equipment (the cellular "switch") and integrate the systems in a way which reduces costs substantially.

Similarly, because they affect the ability of operators to regionalize their systems, RSA licensing policies will help to determine whether "handing off" calls from one system to another is a simple or a difficult task. If hand off is made too difficult, non-wireline cellular customers would lose service as they cross the MSA-RSA boundary—necessitating redialing and experiencing potentially disruptive revalidation procedures to reestablish the call.

In addition, licensing standards will affect how quickly the cellular industry can bring affordable, high quality service to the public. A policy that allows a flood of RSA applications from inexperienced operators and speculators, for instance, will inevitably create processing delays and is likely to place many RSA authorizations in the hands of lottery participants who are unable to build systems and provide service in the foreseeable future. Operators who are capable of initiating service, in turn, would be forced to incur considerable time and expense in acquiring these systems from the lottery winners. Not only would the provision of cellular service to subscribers then be delayed, but the cost of that service to the public would also increase.

The RSA licensing debate thus does not simply concern which companies should be able to compete and make profits in the cellular marketplace. On the contrary, it raises critical issues about the availability of affordable, reliable cellular service to rural Americans.

THE RSA PROBLEM

The impending RSA problem is simple to describe—a potential, massive overloading of the rural cellular application processing system by tens of thousands of lottery ticket holders leading to substantial delays in initiation of service. If existing qualifications policies are maintained, the Commission can expect to receive more than 200,000 applications for the non-wireline authorization in the 423 RSAs. The great bulk of this flood of paper will have been produced by "application factories" marketing the cellular telephone lottery.

The FCC's experience with the MSA applications illustrates the serious problems and delays which arise when an avalanche of applications overwhelms the agency's processing capabilities. The Commission received nearly 100,000 applications for cellular systems in the 305 MSAs, almost all seeking the non-wireline authorization. The number of applications per market grew dramatically over time, as the business of packaging and mass marketing lottery applications became a growth industry.

The numbers tell a dramatic tale. The FCC received approximately 334 applications for markets 31 to 60 and 567 filings for markets 61 to 90. At the time, those figures appeared to be a burdensome processing problem which the newly enacted lottery would rectify. Subsequently, in July 1984, more than 5,000 applications were filed for markets 91 to 120. Today, in Janury, 1988, some of these markets still await the first issuance of a non-wireline construction permit.

And, the deluge grew even more with subsequent rounds of filings, despite the fact that the applications were for increasingly smaller cellular markets: In February, 1986, the FCC received over 15,000 applications for markets 121 to 150, in March over 6,000 applications were submitted for the 15 markets from 151 to 165, in April more than 33,000 filings came in for the 75 markets from 166 to 240, and in May over 38,000 requests were made for the last 65 MSAs. When the dust had settled at the FCC, it became clear that for the 90 largest MSAs an average of about 10

applications per market were received, while the 85 smallest markets averaged 536 applications each.

That application processing delays would result from this inundation was unavoidable. Equally inevitable was the fact that the consequences of these events would fall primarily on the non-wireline cellular providers. Wireline cellular markets were established with eligibility restrictions so that only local telephone companies could apply. As a result, only a few wireline applications were received for any given market and settlements generally were reached quickly. Thus, one year after the last of the application filing dates, 61 non-wireline construction permits had been issued in the 185 MSAs above 120, leaving 124 markets unprocessed. At that same point, 122 wireline permits had been issued for those 185 MSAs, exactly twice the non-wireline number.

This process has seriously impaired the competitive marketplace sought by the FCC. In many communities the benefits of a two-supplier competitive marketplace were denied for an extended period. Importantly, the harms caused by the wireline head start do not disappear the day the non-wireline system begins operation. The advantages of many months of monopoly access to the pent up demand in a market can be overcome only over the course of years in many cases. While non-wirelines can resell wireline services, resale is a costly and ineffficient way for non-wireline companies to mitigate the harm caused by the wireline headstart.

It also is important to note that the story of delay does not end with the issuance of the construction permit. The massive number of non-wireline filings led applicants to enter large settlement groups for risk sharing purposes. However, partnerships with as many as 400 members or more proved unworkable when it came time to fund and build a system. The result was many more months of delay as ownership consolidations were negotiated.

It is beyond debate that the events I have described have harmed the public interest. Realization of the FCC's two primary public goals for cellular—early initiation of service and an effective competitive marketplace—has been significantly impaired. My company and I share the FCC's goals and hope that some means can be devised for preventing a repetition with the rural cellular filings.

There is every reason to believe that unless changes are made in eligibility standards, a "gold rush" mentality will occur. Applications are available in large quantities for relatively low cost, with large scale campaigns underway to convince individuals to file. Under current procedures the only significant cost incurred before the lottery is completed, other than the application preparation expense, is the $200 filing fee. There are no legal fees, loan commitment obligations or other expenditures required. In fact, one firm is advertising a package which includes all application preparation, FCC filing fees, microfilming and federal express costs for all 423 RSAs for a total price of $11,000. For that investment, the firm will group you in a joint filing with others who have paid the same amount.

The relatively low cost of entering RSA lotteries is being touted as "truly a once-in-a-lifetime opportunity to strike it rich", as possibly "the greatest return on investment ever offered" and as a "government lottery which is being held to *give away* the exclusive and very valuable cellular telephone franchises." Advertisements also claim that "a 2% ownership in a city of 150,000 could be worth over $150,000 at maturity in 7 years." Potential applicants are being told that by joining an alliance of filers applying in all RSAs, "the most likely event is that ownership interests in three licenses will be obtained.

The extensive circulation of these advertisements, and the many months of marketing, make it certain that the number of RSA applications will a least be as great as with the MSAs. The adverse consequences to the public interest will be even greater.

As I have noted, there are at least four potential harms to the public from a repeat of the free-for-all filing policies employed in the MSAs. There are (1) delays in service, (2) less efficient service, (3) more costly service and (4) denying the public the advantages of a competitive marketplace. The botton line is that a replay of the MSA processing system in the RSA markets will seriously disserve the public.

RSA REALITIES

The adverse impact of the impending RSA lottery problems is heightened by the harsh economic realities associated with serving sparsely populated rural areas and the "hype" generated by the application mills. Although RSAs are heavily advertised by application factories as future gold mines, a realistic assessment suggests that they will be difficult markets to develop. RSAs typically have small populations

scattered over large geographic areas. The average RSA has just over 140,000 inhabitants, with some RSA populations ranging as low as 12,000.

Despite their small and dispersed populations, providing cellular service to RSA subscribers will require a tremendous capital investment. Conservative estimates put the cost of engineering, installing and testing a simple two cell turnkey system in the range of $1 million. A switch alone costs at least $500,000, and must be operated by an experienced technician. Moreover, the working capital needed to operate such a system amounts to an additional 30 to 40 percent of total cost. McCaw's own experience suggests that a cellular operator would need to spend over $1 million to build and operate just a single cell system in a small RSA in the first year.

Despite such extensive capital requirements, the potential return on an RSA investment can be extremely limited. Industry sources report that, five years after initiation of service, sixty percent of all RSAs are projected to have fewer than 1,500 subscribers for both wireline and non-wireline operators combined. Thrity-seven percent of the RSAs are projected to have a total demand in the fifth year of less than 1,000. These subscribers, moreover, are likely to be spread across broad territories. Thus, by any rational standard, RSAs will prove to be marginal businesses if operated on a stand alone basis.

MC CAW AND THE NON-WIRELINE CELLULAR INDUSTRY'S CONCERNS ABOUT RSA LICENSING POLICIES

Neither McCaw nor any other non-wireline cellular carriers would be interested in owning and operating most RSA systems as stand alone systems. Instead, McCaw's primary concern in addressing the RSA problem is in developing cellular's potential and competing as a matter of necessity with wireline carriers operating on a regional basis. Let me review those specific concerns for you in detail.

First of all, it must be recognized that under the wireline set aside, telephone companies such as the Bell Operating Companies are virtually guaranteed the ability to construct regional systems including the RSAs in their territory. This occurs because the eligibility restrictions imposed under the wireline set aside only permit a few entities to file for a given RSA. Telephone companies have already been meeting to discuss full settlements for RSA markets. Thus, one can anticipate that by the time lotteries might be held, the wirelines will already have market settlements that remove any uncertainties or delays in the licensing process.

In contrast, the competing non-wireline carriers like McCaw will be left in a hopeless morass caused by tens of thousands of applications being filed for non-wireline authorizations. In the RSAs, this means that wireline carriers will have an enormous headstart in signing up the limited number of prospective cellular subscribers—further undermining the competitive viability of the ultimate non-wireline licensee.

It also means that wireline carriers have assurances that they will receive RSA licenses needed to fill in gaps in their coverage of key interstate highways in order to provide wide area coverage. Indeed, the wirelines can achieve these goals without the enormous expenses associated with acquiring RSAs from permit or license holders as McCaw and the non-wirelines must do.

McCaw and the non-wireline industry must necessarily be concerned with these advantages accruing to wireline carriers. McCaw cannot compete effectively without having similar quick entry into the RSA business and similar regional capabilities. For example, in the state of Washington, the RSAs would account for very few cellular subscribers. Roughly 75 percent of the state's population live in the MSAs and only 25 percent reside in the state's RSAs. Nonetheless, a wireline marketing campaign in Seattle—where the core business exists—touting the wireline's regional coverage in comparison to a smaller McCaw service area could have severe adverse effects. Seattle subscribers might well choose the wireline carrier just in case they someday will be driving into areas served solely by the wireline. As a result, McCaw's interest in the RSAs' fate is a matter of utmost competitive importance.

The problem would be less severe if any speculative applicant could be relied upon to build a high quality system promptly. Experience, however, suggests that this is unlikely. Past lottery winners have been slow to build and often select less sophisticated switching systems that are not compatible with adjoining cellular systems, such as those constructed by McCaw.

The practical effect on the public, as non-wireline subscribers, is simple to explain and understand. As the cellular customers cross boundaries between adjoining cellular systems, they lose service in the middle of their calls. If the adjoining system is not yet operational, continued service is impossible. And, if the adjoining system is operating with incompatible equipment, the subscribers suffer the inconvenience of

having to redial and to be revalidated on that system. The net result is poor service and an unhappy customer for non-wireline carriers.

Finally, it bears noting that the economics of RSAs also change if RSA cellular systems are owned and operated by licensees serving adjacent MSAs. An RSA and its adjacent MSA can share a switch, thus saving the cellular operator the considerable costs of purchasing and operating a separate switch. In addition, the RSA can be integrated into a regional network which ties two or more cellular markets together into a single service. McCaw's experience reveals that such regionalization has allowed carriers to realize pronounced economies of scale. Automatic roaming becomes feasible, discounted volume purchases are possible, joint marketing efforts can be undertaken, and administrative functions such as billing, maintenance and surveillance can be centralized. Indeed, in a number of situations, regional carriers will be able to serve RSAs from adjacent MSAs without even erecting expensive cell sites in the RSAs themselves.

The benefits to the public of licensing RSAs to adjacent MSA operators are clearly substantial. The economic efficiencies realized from joint operation will inevitably result in lower cost service to cellular subscribers. Moreover, by enabling regional carriers to forego the initial costs of considerable capital investments and operating expenditures, those carriers will be able to bring quality cellular service to the RSA public much more quickly. Lower costs and faster advent of service, in turn, will increase the ability of regional non-wireline carriers to compete with regional wireline operators.

THE FCC'S EFFORTS TO DATE TO REMEDY LOTTERY PROBLEMS

In seeking Congressional action, McCaw is by no means being critical of the FCC's performance to date. To the contrary, we want the FCC to be given better tools to deal with RSA lottery problems. While we may differ in our respective assessments of the best means for solving the RSA problem, McCaw shares with the Commission the common overriding goal of ensuring the fastest possible availability of cellular service under pro-competitive marketplace conditions.

The FCC, in fact, has worked diligently to struggle through the flood of MSA applications. The Common Carrier Bureau and its Mobile Services Division staff has done a commendable job of fashioning sensible approaches to dealing with the unanticipated and ever increasing volume of MSA applications. FCC Chairman Patrick also has worked to develop a sound regulatory framework for cellular's future. Under his leadership, the Commission has worked to weed out unqualified lottery abusers while adopting flexible policies governing transfers of cellular interests.

In its *Madison Cellular Telephone Company* decision, the Commission recognized the emerging realities of the cellular business. First, the decision noted that non-wireline carriers were being driven toward "multi-MSA" cellular systems in order to compete with wide area systems of the Bell Operating Companies. Second, the decision noted the economic benefits accruing from integration of an MSA into a regional network, factors such as reduced costs attributable to sharing of switches, personnel, and administrative overhead. The Commission also observed that many permit holders waited until the last possible time to build their systems and then opted for inexpensive, low quality equipment. Most importantly, the Commission concluded that, against this backdrop, restrictions on transfers of permits would frustrate the overriding goal of achieving "[t]he rapid and efficient provision of cellular service to the public." Accordingly, the Commission wisely adopted a policy of allowing *bona fide* applicants to transfer their interests.

McCaw strongly supports the Commission's *Madison* policy. Indeed, flexible ground rules for transfers have been an indispensable mechanism for redressing and rectifying some of the delays and uncertainties in the MSAs. They have equal relevance and importance to RSA processing. Thus, these policies should not be disturbed or altered in evaluating other added measures to resolve the impending RSA problems.

SOLVING THE RSA PROBLEM

Absent Congressional action, the stage is now set for a chaotic filing period for cellular RSAs. Several hundred thousand applications will clog the FCC processes. Investors enticed into buying turnkey lottery tickets will discover to their dismay the harsh economic realities of the RSA market-place. Serious, committed service providers from the non-wireline industry will once again be left at the starting gate by their wireline competitors' headstart advantages. The net result would be a serious disservice to the public and the cellular industry.

A wide variety of options have been identified as potential solutions to the RSA problem. They include increased application fees, strengthened financial showing requirements and other similar policy changes. While these measures would have some salutary effects, without additional actions they would only marginally improve current processing procedures. Their principal defect is the ability and creativity of application mills in ferreting out solutions to FCC filing requirements on behalf of their lottery ticket holders. Thus, McCaw believes that the real solution lies elsewhere.

As I noted earlier, during the last session of Congress considerable attention was focussed upon a proposal designed to prevent such problems. The proposal would establish qualification showings for applications seeking FCC licenses for non-wireline cellular telephone systems in RSAs. Under this proposal, RSA licenses would be open to common carriers holding cellular licenses in the larger adjoining MSAs and two-way mobile carriers already providing certain levels of service in the RSA. The proposal was intended to ensure that cellular systems in rural areas will be built and operated in a timely manner by operators who have already proven their commitment to the prompt provision of cellular service. At the same time, the proposal would increase the current level of competition in the cellular industry by ensuring strong, effective competitors to wireline cellular systems owned by telephone companies such as the Bell Operating Companies. The proposal thus sought to promote competition *and* ensure the faster availability of cellular service to unserved rural Americans.

McCaw strongly supports this proposal for several overriding reasons:

First, The Advent of Cellular Service Rural America Will Be Delayed as Lottery Ticket Holders Flood The FCC's Current Processes. When licensing non-wireline systems in the MSAs, the FCC was inundated with applications from parties with no experience in providing telecommunications services. As the Commission struggled to process the paperwork, the headstart enjoyed by the wireline carriers grew. The flood is likely to be even greater for the RSAs, with several hundred thousand non-wireline applications expected. Failure to adopt eligibility limitations to control their number would only delay non-wireline service to rural Americans and increase the competitive edge already held by the wireline operators.

Second, The Use of RSA Eligibility Showings Is Consistent With Past Actions Designed To Expedite Service To The Public. The FCC has previously used comparable eligibility limitations to promote fast, efficient cellular service to the public. In creating a regulatory framework for cellular telephone service, the Commission decided that there would be two competitors in each cellular market, a telephone (or "wireline") company and a non-wireline carrier. The Commission set aside one system per market for local wireline telephone companies because it concluded that only the telephone companies possessed the expertise and resources needed to address immediately the public's considerable demand for cellular service. Eligibility requirements for non-wireline applicants in rural areas would serve the same purposes: they would ensure that the companies most qualified and best prepared to provide cellular service would in fact do so.

Third, RSA Eligibility Showings Would Increase Competition. The proposed eligibility requirements would promote competition by providing well-financed, experienced and expeditious alternatives to wireline cellular service. This approach would avoid past wireline advantages by applying comparable qualification requirements and eliminating any headstart advantages due to the numbers of potential applicants. The need for viable non-wireline competitors is particularly critical in rural areas, which are by definition large territories with scattered populations and uncertain cellular demand. Should nonwireline carriers without adequate resources and expertise be permitted to enter such marginal service markets, they could well fail (even if they are eventually built), leaving the public without any competition at all.

Finally, RSA Eligibility Systems Would Ensure That Cellular Service Could Be Provided More Efficiently To Sparsely Populated Rural Areas. RSAs, on a stand alone basis, are marginal markets. However, as noted above, these systems constitute important fill-in components of emerging regional non-wireline networks. By sharing switches, personnel and overhead with adjoining MSA operations, faster, cheaper service can be brought to the American public.

CONCLUSION

In conclusion, I would once again like to thank the Subcommittee for affording me and my company the opportunity to participate in these important deliberations. The stakes here for the American public are direct and substantial—the availability

of cellular technology to rural residents of this country. The problem is readily evident—how to deal with an impeding deluge of applications incited by promoters who have characterized RSAs as a government giveaway of valuable licenses. McCaw, for one, believes that the best, most straightforward solution to this problem is an eligibility showing for non-wireline applicants patterned after the past wireline set aside.

On behalf of McCaw Cellular Communications, Inc., we look forward to assisting the Congress in evaluating and acting upon the record compiled in this proceeding. We would be pleased to provide whatever information you require or answer whatever questions you may have.

Thank you for your time and attention.

QUESTIONS OF SENATOR PRESSLER AND THE ANSWERS

1. Why should rural providers be subject to rules and costs that drive up the cost of service that did not apply to MSA's.

Our goal was to insure that a licensing process was developed that provided a lower cost to both the rural provider and, more importantly, the rural consumer. We would argue that in a vast majority of the cases, the RSA can be served most efficiently and expeditiously by the adjacent MSA operator taking advantage of the equipment he has in place and the other economies of scale his operation provides. The MSA licensing process is proof that the lottery winner is merely a speculator who intends to sell his license to a legitimate operator. The adjacent operator is the only logical buyer who must have the RSA license to compete effectively against his RBOC competitor. If he is subject to the same rules used in the MSA, he will incur significant capital costs to purchase the license from the lottery winner. This is a cost the wireline competitor does not have, and that must be born by the rural consumer.

2. If RSAs adjacent to MSAs are likely to be the most lucrative, and if those are to be arbitrarily given to the companies serving the MSAs, isn't that a reward for those large companies to the detriment of the rural companies?

Only a handful of RSAs, adjacent or non-adjacent will be lucrative let alone operate at break-even. The cost of constructing a stand alone RSA system will be in the range of $500,000 to $1 million. A recent study projected penetration in the fifth year will less than 1%, or roughly 1,200 people. The revenue generated by these subscribers would never amortize the cost of construction.

Conversely, the adjacent MSA operator who has already made a very substantial capital investment in equipment, staff and the establishment of a marketing network, can serve the rural area at a fraction of the cost.

Congress originally established the duopoly to provide for two viable competitors and a choice for consumers. We are not asking for a reward, merely an equal playing field among competitors.

The rural wireline companies, who are <u>given</u> their licenses outright have every opportunity to serve <u>rural</u> Americans quickly and efficiently regardless of whether MSA operators receive the adjacent license. If they feel we would have any headstart, we would suggest the issuance of simultaneous construction permits and mandatory reselling until both systems are operable.

3. Doesn't the dual lottery proposal retain all the problems of speculation in the first stage of the process, where the rules are the same as now?

Yes, we would argue in the case of a dual lottery that stricter financial showing also be established for applicants as a means of discouraging the speculator. We have come to realize in this process that attempting to achieve a consensus is extremely difficult when operators and speculators are so far apart.

The dual lottery proposal was one that insured that in every case there was going to be a legitimate operator at the table with the lottery winner. It also did not limit the "entrepreneurs" opportunity to participate.

4. Do you have any alternative proposals for limiting speculation without eliminating serious competitors or putting undue burdens upon their involvement?

The problem we have is fashioning a proposal that can determine who is a speculator and who would become a serious competitor. Our experience in the MSAs taught us, that although many lottery winners originally intended to build, they realized the cost of construction and operation as well as the long term nature of reaching profitability. We do feel that strengthening financial showing will at the very least decrease the number of applicants. We know that the most effective way to operate an RSA in almost all cases is to run it off the equipment in place in an adjacent MSA.

At the urging of both the chairman and the minority we have met numerous times since our hearing to try to find a consensus that everyone can agree upon and still addresses all of the concerns. Again we have determined pre-lottery financial showing to be an effective way to deal with speculation. The applicants have realized the value in being able to deal with us as it relates to roaming, handoff and switch sharing if they do intend to maintain ownership of the RSA license. With this in mind we have reached a consensus that although imperfect would meet some of these objectives. The proposed consensus is as follows:

- Adjacent MSA operators or conventional mobile telephone operators doing business in the RSA would as a group own 20% of the RSA license.

- The lottery applicant would be subject to strengthened pre-lottery financial showing.

- The lottery winner would become the beneficial owner of the remaining 80%.

- A right of first refusal would exist between the two owners.

- If either owner were unable to make his capital contributions, the other owner would be able to do so and have his ownership increase proportionately.

This alternative ensures the entrepreneur the opportunity to work with the adjacent operator and take advantage of all of the economies of scale provided by his existing system. Further, it allows the MSA operator the ability to compete effectively with the wireline cellular provider. It gets service to the rural consumer expeditiously and at the lowest possible cost. And, if the lottery winner is unable or elects not to operate the system, the rural consumer is protected by the presence of an experienced cellular provider.

We hope this alternative is able to move quickly and gain broad based support. We now have a very diverse coalition moving toward the same end, and we are very encouraged. We appreciate the opportunity to both testify in the hearing and respond to these questions.

Senator INOUYE. Thank you very much, Mr. McCaw.
Our next witness is Mr. E. William Henry.
Mr. Henry.

STATEMENT OF E. WILLIAM HENRY ON BEHALF OF THE UNITED STATES INDEPENDENT CELLULAR TELEPHONE ASSOCIATION

Mr. HENRY. Thank you, Mr. Chairman.

I am a member of the Washington, D.C. law firm of Ginsburg, Feldman and Bress, and I am here to testify on behalf of the members of the United States Independent Cellular Telephone Association, known as USICTA, whom we represent.

I understand that you will admit my written statement into the record, and I thank you for that.

USICTA is a trade association of independent small businessmen and women located throughout the country who plan to apply for cellular telephone construction permits in rural service areas. These areas are commonly called RSAs. At stake in these hearings is one of the fundamental tenets of U.S. telecommunications policy developed in over 50 years of regulation under the Communications Act. This principle is the concept of open entry in which all qualified persons have the opportunity to develop emerging technologies by becoming FCC licensees.

Open entry has made possible private international satellite systems, private transoceanic fiber optic cable systems, and private teleports for satellite transmission and reception. It has allowed people like my co-panelist, Mr. Neff, to apply for, construct and operate cellular telephone systems. Open entry has also led to diversified ownership in the broadcasting industry and long distance common carrier industry.

In short, our telecommunications policy has always accommodated small businesses, and in addition, affirmatively encouraged and nurtured small business entrepreneurs by providing them with opportunities to grow and prosper.

USICTA, therefore, is committed to maintaining open entry at the FCC for its members and for all other RSA applicants, large and small alike. It views current proposals for closed entry as radical departures from this demonstrably beneficial policy and therefore unwise and unwarranted. These proposals in our view represent a land grab of valuable spectrum space by entrenched licensees, and I will get into this a little bit later. We think in particular the system—the scheme—mentioned by Mr. McCaw is really a numbers game and is without any fundamental principle behind it.

Although there is no legislation now officially pending on this subject, Members of this subcommittee and other Senators have expressed concern about potential abuse of the open entry process by speculators who seek only a quick profit and have no interest in constructing or operating cellular systems. As a result, unofficial legislative proposals are under active discussion, all of which involve either some form of closed entry or, as Mr. McCaw mentioned, a two-tier lottery system weighted heavily in favor of existing cellular licensees.

USICTA members share this concern about speculation. They believe, however, that these proposals, these legislative proposals so

far under discussion, if adopted, would either fail to eliminate speculation or do so in a manner that greatly disserves the public interest. The reasons for this conclusion are set forth in some detail in my written statement submitted today.

In a nutshell, however, USICTA's basic point is that all of these proposals are highly discriminatory against small business, including minority owned businesses, and none assures that the RSA cellular systems will be built quickly or that such systems will be more economically or technologically efficient.

All are, in effect, private relief bills that would hand out over $1 billion to a few major companies, primarily McCaw Communications, the principal advocate for and beneficiary of these proposals.

For these reasons, USICTA strongly opposes all of them.

One aspect of the closed entry or weighted lottery proposals advanced by McCaw and others deserves special attention even in this quick summary. All of them assume that non-wireline stand-alone RSA systems, those systems owned and operated by independent companies, unaffiliated with a neighboring MSA system, will be so economically disadvantaged in the competition with wireline companies that they will be unable to get off the ground or, once in operation, be unable to survive. The public in that scenario is the loser.

This assumption, USICTA believes, is false. With your permission we plan to submit a written statement on this subject before the record of these hearings is closed. For now, let me just say that this issue of economic viability can be addressed only on a case-by-case basis because the geographic, demographic, topographic, and other relevant factors differ so greatly from one country to another. What can now be said with confidence, however, is that any claim that all or most RSAs will not support technically efficient, cost effective, quality service, stand-alone systems is itself speculation and entirely without concrete, factual support.

On a positive note, USICTA believes that steps can be taken if deemed necessary to drastically reduce or eliminate speculation. These steps are fully in keeping with an open entry policy and would promote the benefits of that policy in the cellular field.

First, we think that the FCC can, if necessary, require cellular lottery winners, as it now requires winners of comparative hearings in the broadcast field, to construct and operate the system for a period of one or more years.

Second, we think the FCC can make clear that the sale of a bare cellular construction permit for profit is not permitted.

And third, we think the FCC can strictly enforce requirements for the timely construction of cellular systems once construction permits are issued.

Thank you very much.

[The statement follows:]

STATEMENT OF E. WILLIAM HENRY ON BEHALF OF UNITED STATES INDEPENDENT CELLULAR TELEPHONE ASSOCIATION

My name is E. William Henry. I am a member of the Washington, D.C. law firm of Ginsburg, Feldman and Bress and am here to testify on behalf of the members of the United States Independent Cellular Telephone Association ("USICTA") whom we represent.

I. USICTA MEMBERSHIP AND OBJECTIVES

USICTA is a trade association of independent small business men and women located throughout the country. USICTA members plan to apply to the Federal Communications Commission ("FCC") for cellular telephone construction permits in rural service areas ("RSAs"). USICTA is committed to maintaining "open entry" at the FCC for its members and all other RSA applicats, large and small alike. USICTA is also dedicated to promoting fair business practices in the cellular telephone industry.

II. USICTA'S POSITION

At stake in these hearings is one of the fundamental tenets of over 50 years of regulation under the Communications Act: the concept of "open entry" in which all qualified persons have the opportunity to develop emerging technologies by becoming FCC licensees. "Open entry" has given us private international satellite systems, private transoceanic fiber optic cable systems and private teleports for satellite transmission and reception. It has allowed people like my co-panelist, Mr. Neff, to apply for, construct and operate cellular telephone systems. "Open entry" has also led to diversified ownership in the broadcasting industry and long distance common carrier industry. In short, the Communications Act has always accommodated small businesses and, in addition, affirmatively encouraged and nurtured small business entrepreneurs by providing them an opportunity to grow and prosper.

The proposals that this Committee is considering to severely restrict "open entry" in the random selection process now used by the FCC to award cellular permits is nothing short of a radical departure from the history of the Communications Act. USICTA believes that this departure is unwarranted and, therefore, strongly opposes proposals for "closed entry." Unfortunately, there is no pending bill to which USICTA can direct its comments. However, at least four different legislative proposals have been advanced informally by proponents of "closed entry." These are:

Restricting entry in the random selection process so that only an operator of a cellular system in a Metropolitan Statistical Area ("MSA") adjacent to an RSA (known as "adjacent MSA operators") would be eligible to apply for that RSA permit;

Holding a "two tier" random selection process in which one applicant would be chosen by lot from among the many applicants for an RSA permit, with that winner then participating in a second lottery in which the only other eligible applicants would be adjacent MSA operators;

Imposing a higher application fee to enter each RSA lottery;

Imposing unduly restrictive financial and technical qualifications to enter the random selection process for each RSA.

Each of these proposals is contrary to the "open entry" letter and spirit of the Communications Act. Each is highly discriminatory against small business men and women who are willing and qualified to apply for, build and operate RSA cellular systems. None would guarantee that cellular systems in the RSAs are built quickly, or that such systems would be more economically or technologically efficient. Rather, as explained later in this testimony, all of these legislative proposals are private relief bills, each one of which would handout over one billion dollars in valuable radio spectrum to a few major companies, including McCaw Communications, their chief advocate and beneficiary.

USICTA believes that no legislation is necessary. What is required, rather, is a return to the "basics" of the Communications Act. In USICTA's view, the FCC already has the statutory authority to, and it should:

Enforce the prohibition in the Communications Act against the sale for profit of a bare construction permit;

Demand timely construction of cellular systems;

Prohibit "trafficking" in cellular systems that have been operated for less than 3 years; and

Foster a competitive marketplace by requiring agreements on "hands-offs" and "roamers" and interconnection of switches among non-wireline cellular carriers that are critical to their ability to serve the public.

If Congress believes that legislation is necessary because the FCC is unlikely to take these steps, USICTA would support a bill which would mandate the above FCC actions. These steps—and not the "land grab" proposed by McCaw and others—would provide a much better solution to alleged problems in the cellular industry.

III. FACTUAL AND LEGAL BACKGROUND

This Committee is well aware of the development of the cellular telephone industry, largely because the industry is barely five years old. The FCC has struggled with the regulatory framework within which this industry should develop. Although it initially used a comparative hearing process to award cellular permits, it eventually moved to a system of lotteries. Some of the details of the random selection process have been changed over the years, but "open entry" has been the basic rule in awarding several hundred permits.

Each applicant has been required to submit an application containing an extensive amount of engineering data about system construction and operation. Upon being selected as the lottery winner, an applicant must provide additional evidence of its basic qualifications. If the FCC is not satisfied that those qualifications have been established—either through its own analysis or as the result of the filing by a third party of a petition to deny the grant of the permit to the winner—then an expedited hearing is held to resolve the issue. If the issue is not decided in favor of the winner, an alternative winner is selected. In short, at the time that it actually awards a construction permit to build a cellular system, the FCC has made certain that the winning applicant is fully qualified to construct and operate.

Not surprisingly, McCaw Communications—as the country's largest non-wireline cellular operator—opposes "open entry" for all qualified cellular applicants. McCaw is attempting to build a national cellular system with several regional centers. Much like the broadcast networks might prefer to own television stations in every major market, McCaw would like to own the non-wireline cellular system in hundreds of MSAs and RSAs. But "open entry" in the cellular industry means that McCaw must enter the random selection process just like everyone else. With over two hundred applicants per MSA—and a like number expected per RSA—McCaw's chances of success are no better or worse than any other applicant.

To build its national system McCaw actively sought out MSA lotttery winners and offered them substantial sums—far above their expenses—to sell bare construction permits or certain rights relating thereto. Indeed, it appears that McCaw may have taken de facto control of some of these unbuilt systems by purchasing a minority ownership interest and an option to purchase a majority interest, along with providing financing or other assistance in the construction stage. Yet the FCC did not act to prevent such de facto transfers of control even though similar actions had previously been prohibited for radio permits, particularly in the broadcasting field.

The FCC's inaction caused the value of an unbuilt system—the mere piece of paper authorizing construction—to skyrocket. Many small businesspeople found themselves deluged with offers worth hundreds of thousands or even millions of dollars for interests in a permit in which they have invested a mere fraction of that amount. Nonetheless, under the existing law, the permit holder was at least required to complete construction of the cellular system and place it in operation before selling full legal title to McCaw.

Unfortunately, however, having already permitted these sales to get completely out of hand the FCC removed virtually all regulation against the for-profit sales of cellular construction permits. In the so-called *Madison* case issued in August 1987, the Deputy Chief of the FCC's Common Carrier Bureau ruled that a bare permit for an unbuilt station could be sold outright for a profit. Thus, McCaw's back-door approach to control—acquisition of minority ownership rights, options and other elements of de facto control—could be abandoned since McCaw would now be able to receive FCC approval for full legal title to permits. Since August 1987 McCaw has aggressively continued its pursuit of unbuilt station permits held by small business men and women. Its legislative efforts regarding the *RSAs* is but a natural extension of its efforts to dominate the *MSAs*.

IV. MCCAW'S "CLOSED ENTRY" PROPOSAL: UNWISE AND UNWARRANTED

About the same time as the *Madison* decision, the FCC was preparing to announce filing dates for cellular applications in the RSAs. The winners were proposed to be selected by the same system of random selection. However, McCaw, concerned about the substantial sums that it was paying to buy out permittees in the MSAs, sought legislation to prevent the FCC from conducting the RSA lotteries. It succeeded in obtaining language in House Report 100-363, accompanying the FCC Authorizations Act of 1987, to limit applicants for the RSA permits to those operators of cellular systems in adjoining MSAs.

The McCaw strategy was clothed, of course, in public interest rhetoric. The McCaw proposal for "closed entry" was said to have these benefits:

the speculative selling of unbuilt stations at huge profits would be eliminated;

economic and technological efficiencies would be realized because RSA systems can best operate from nearby MSA switches; and

construction in the RSAs would be completed sooner because an adjacent MSA operator has proven construction experience and is clearly financially qualified.

During the course of the Senate's deliberations on the Budget Reconciliation Bill and the Continuing Resolution, McCaw urged that the language contained in House Report 100-363 be enacted as a statutory requirement. The Senate, led by the Chairmen of the Commerce Committee and this Communications Subcommittee, refused to adopt the House Report language. Rather, the FCC was directed to wait 90 days before accepting RSA applications so that Congressional hearings could be held to explore the issues raised.

A. Fundamental Flaws in the McCaw Proposal

McCaw's proposal for "closed entry" in most of the RSAs is a radical departure from the history of the Communications Act. Never, since the Act's adoption, has Congress limited eligibility for a license to an existing licensee—particularly one in an adjoining geographic area. Even the thought of reserving broadcast or satellite licenses, for example, for present licensees—thereby excluding small and minority owned businesses—would be dismissed as grossly unfair and anticompetitive. The McCaw proposal should be viewed as no less drastic a departure from appropriate means of achieving public interest goals. Not only is "closed entry" in the RSAs a bad idea in principle, but the assumptions and conclusions upon which it is based are fundamentally flawed.

The "speculative" selling of permits was caused in substantial part by McCaw and others offering enormous prices for unbuilt stations and by the cooperation of the FCC in allowing the de facto and de jure transfer for profit of these unbuilt stations. The solution is to require the FCC to return to the long-standing prohibition against the for-profit sale of construction permits. Moreover, as demonstrated by many small businesspeople who have become cellular permittees as the result of the random selection process, many applicants are genuinely interested in building and operating their systems, and not in selling a bare permit. There would undoubtedly be many more examples to point to here if the law had not been twisted beyond recognition to permit McCaw and others to gobble up bare permits at enormous profit to the sellers.

According to USICTA's engineering analysis, in very few cases would economic and technological efficiencies be realized in the RSAs through the proposed integration of RSA systems with switches in adjoining MSAs. Initially, it is a myth that "stand-alone" cellular systems simply cannot thrive economically in the RSAs without being connected to a neighboring MSA switch. Likewise, it is untrue that RSA non-wireline cellular operators will not be able to compete with RSA wireline cellular operators unless the RSA system is owned by an adjacent MSA operator. Further, none of the "cosed entry" legislative solutions gives even reasonable assurance of the realization of any operating efficiencies in the overwhelming number of RSA markets that would be closed to applications from small businesspeople. A better solution would be to require an adjoining MSA operator to interconnect an RSA operator—whoever that might be—with the MSA switch in the small number of cases where efficiencies can be realized and to enter into "hand-off" and "roamer" agreements with that RSA operator.

The Commission has rules in place to assure that RSA applicants are financially and technically qualified. The Commission can change these rules as long as they are not unduly restrictive. Moreover, the Commission has authority to insure that construction proceeds within the required timetable, including the ability to require substantial progress towards construction during the term of the permit.

V. PROBLEMS WITH SPECIFIC "CLOSED ENTRY" PROPOSALS

None of the four specific "closed entry" proposals described at the beginning of this testimony comes close to solving the alleged concerns about the random selection process. Moreover, the price to be paid in the implementation of any of these proposals is unjustifiably high in terms of other public interest considerations.

A. McCaw's Proposal: Restricting Entry to Adjacent MSA Operators

McCaw's proposal, described in the House Committee Report, is seriously flawed for the reasons set forth immediately above. Restricting eligibility for an RSA permit to adjoining MSA operators would close off 85% of the 423 RSAs containing 91% of the total RSA population. Only 63 RSAs, or 15% of the RSAs, have no adjoining MSA operator. While this proposal would eliminate spectaculars, it would do

so at the price of also eliminating all of the applicants genuinely interested in building and operating a system. Moreover, there is no basis for concluding that it would bring economic efficiencies to more than a handful of the closed RSAs. In many cases, the swtich in the adjacent MSA would literally be hundreds of miles away, thereby introducing greater economic costs and technological uncertainties like loss of reliable signal quality. LIkewise, contrary to McCaw's conclusory assertions, nonwireline MSA cellular operators can compete effectively with their wireline cellular competitors without owning regional systems that include RSAs; nor must RSA systems be owned by MSA operators to thrive.

Nor does an adjacent MSA operator necessarily have the resources to make rapid RSA construction a priority in its MSA-based system. According to an article in the January 18, 1988 issue of *Radio Communicating Report*, McCaw has been operating at a substantial loss. Metro-Mobile, another major MSA operator, took almost three years to complete constructin and commence operation of its three systems in Connecticut. Thus, it is speculative and contrary to intuition to believe that operators like McCaw or Metro-Mobile—given their own construction and financial problems in the MSAs—are more likely to provide service in the less populated RSAs faster than a small businessperson whose only system is in an RSA.

Finally, the price to be paid for restricting eligibility is unreasonably high. This form of "closed entry" is not only unprecedented and prejudicial to *bona fide* applicants, it is worse than an auction because it gives away spectrum to a few large companies at prices well below the market value of the spectrum. This "closed entry" would also result in the loss of millions of dollars to the Treasury in the form of application fees that are now collected through "open entry."

One variant of the above proposal that we have heard discussed is to retain "open entry" if an RSA abuts zero or one MSA, but to have "closed entry" if two or more MSAs are abutted. This would still close 58% of the RSAs containing almost 70% of the RSA population. Moreover, there is no principled justification for a cut-off based on two adjacent MSAs. For the same reasons discussed above, this proposal does not guarantee any quicker, more reliable, more econoic or more efficient RSA service than would be provided by an independent businessperson who does not own an adjacent MSA system. LIkewise, this proposal is flatly contradictory to decades of "open entry" practice under the Communications Act.

B. Two-Tier Random Selection Process

This proposal has most of the problems of an MSA adjacency requirement and raises additional concerns. Its dubious "virtue" is that it would serve many of the private interests that are battling over the issue of RSA eligibility; that is, by allowing small businesspersons to file applications in all 423 RSAs, this proposal serves the private interests of law firms and engineering firms which profit from mass filings. Thereafter, however, applicants are left out in the cold to take part in a second lottery against adjacent MSA operators where their chances of winning in most cases will be substantially less than their adversaries.

Further, there is no principled justification for this two-tier lottery process. If the independent businessperson refuses to reach a settlement with adjacent MSA operators, the probabilities are that 58% of the RSAs will go to adjacent MSA operators in the second lottery. Where independent selectees are willing to settle with adjacent MSA operators to avoid the second lottery, such independents will be relegated to minority ownership interests.

Moreover, this two-tier proposal may actually encourage speculation because a first tier winner knows that for all practical purposes he or she can, if desired, count upon a settlement with an adjacent MSA operator. Further enough has been said to demonstrate that not only is this proposal unfair and contrary to the public interest, but it would also be somewhat complicated to administer.

C. Substantially Higher Application Fees

Any proposal to charge significantly higher application fees would not solve the problems alleged to exist with the random selection process. Moreover, it is the practical equivalent of an auction that makes spectrum available only to the wealthy. It would also be a major shift in the "open entry" philosophy of the Communications Act.

Cellular applicants must now pay a $200 application fee. There has never been any claim that the fees collected do not cover the expenses of processing applications. To raise the application fee to $500, for example, would hardly deter true speculators, and any resultant drop in applications could actually result in lost revenue to the Treasury. Although an application fee in the range of $5,000 or higher might deter many speculators, it suffers from the same problem as the proposal to

restrict entry to adjacent MSA operators: a high fee does not mean that the applicant can provide economic, efficient and rapid service. Moreover, this high fee, accompanied by the high risks of a lottery, would effectively foreclose the small businessperson from applying. In addition, the concept of high fees that do more than recover processing costs would logically apply to all communications applications, not just those in the cellular area. Finally, the requirement of a high fee is really an auction in disquise, with one key difference: there is, in effect, a "cap" on the price to be paid for the spectrum. This is hardly in the public interest.

D. Unduly Restrictive Financial and Technical Qualifications

The final suggestion of which we are aware is that Congress should mandate stringent financial and technical qualifications for RSA cellular applicants. USICTA strongly supports the general principle that all permittees should have the requisite financial, technical and other basic qualifications. No less is required under Section 308 of the Communications Act. It is unnecessary, however, for Congress to impose special obligations on RSA applicants.

The Commission has ample authority to assure that a permittee possesses basic qualifications. It also has the expertise to refine those qualifications. For example, applicants could be required to set forth a construction plan and a timetable for construction. If such changes are necessary, the Commission should be allowed to propose them before Congress acts.

In addition, some of the legislative proposals made by private parties simply do not make much sense. To say that applicants must have a minimum net worth or minimum gross income would allow applicants with substantial operating losses—like McCaw—to receive cellular permits, while wealthy individuals and highly profitable small businesses might be precluded from filing applications. As to technical qualifications, the construction of cellular systems is not very difficult compared to many other types of facilities for which the FCC issues authorizations, such as satellites and television stations. In addition, the cellular industry is only about five years old. To limit RSA cellular applicants to those entities with prior cellular experience is both unnecessary and imposes unfair barriers to entry in this still-developing industry. Moreover, given the short life of the cellular industry to date, all non-wireline operators' experience is limited at best.

In short, USICTA opposes any legislative proposal that imposes special, more stringent qualifications on RSA cellular applicants than generally exists in other communications fields.

CONCLUSION

For the above reasons, USICTA strongly opposes legislative proposals for "closed entry" in the RSAs. Rather Congress should insist that the FCC return to the basics of the Communications Act by prohibiting for-profit sales of bare permits, prohibiting trafficking in newly-built and operating systems and by requiring timely construction. These step can prevent speculation and issure rapid service in the RSAs. If the FCC refuses to take these steps Congress can mandate that it do so.

Senator INOUYE. Thank you very much, Mr. Henry.
Our next witness, Mr. Steven S. Seltzer.

STATEMENT OF STEVEN S. SELTZER, PRESIDENT, MODERN COMMUNICATIONS CORP.

Mr. SELTZER. Thank you, Mr. Chairman and Members of the subcommittee, for allowing me this opportunity to speak on behalf of many of the radio common carriers currently serving rural America.

At the age of 32 I have spent over 50 percent of my lifetime growing up in a family-owned business that provides conventional mobile telephone service. During this time, our family and our firms have invested substantial sums of money and time to bring quality mobile telephone service to the areas that we serve.

I think it is important that we look at mobile telephone service and conventional service. Back in the late 1940s, manual service became available where all calls were placed through an operator.

In the 1960s, the format known as improved mobile telephone service, or IMTS, became available, and many RCCs, at great expense, gravitated to that type of a standard.

Conventional service today is direct dial to and from the vehicle. In most cases it is wide area. We have built an extensive roamer network, and we have the ability to provide hand-held or portable communications.

What conventional mobile service lacks is sufficient channels or spectrum to continue providing quality service to the growing population of mobile telephone users. Recognizing this limitation and the need for additional channels, a high capacity mobile telephone service, cellular, was developed. While this was going on, many mom and pop operations such as ourselves were busy investing and building in a conventional network of mobile telephone systems that cover much of rural America.

Over these past 40 years, firms such as ourselves have developed the experience, expertise and everything we need to help provide rural America with quality cellular mobile telephone service. We know the terrain, we know the markets, and we have the local presence to get the job done, and get the job done efficiently and economically. We have access to or own prime transmitter sites. We have already built and grown our own small companies in the markets that we have, and we are able to install and service cellular as a natural outgrowth of our existing mobile telephone business.

Many RCCs such as ourselves are now faced with an inability to grow and continue expanding our service. This is due to that lack of channels that I mentioned that are compatible with our existing systems. Cellular is the only logical path for us to pursue in order that we can continue providing mobile service.

With the rules that currently govern the RSAs, small RCCs such as ourselves are literally going to pay ransom rates to a lottery winner to get the cellular frequencies we need to continue in business. RCCs are being asked to pay literally millions of dollars to speculators who have no real interest in the provision of quality mobile service to rural America. In my opinion, this is a gross injustice to those of us, like myself, who have helped Americans' communicate with mobile telephone service over these past 40 years.

And I would have to say that ultimately the public, you and me, and everyone in this room, are going to pay the price.

This morning on Good Morning, America, Steven Aug mentioned today's hearing and the lottery process, and the licensing mills specifically. Perhaps he put it better than I can. In the present system of making service available to the public, the only real winner is going to be the application mills, not the public.

I urge your committee to consider all aspects of this important situation and do everything within your power to bring service to the public. The firms such as ourselves are qualified to bring quality service to the public at the lowest possible cost. Carriers being forced to pay exorbitant rates to gain these licenses will have no alternatives but to pass these costs on to the public.

Thank you.

[The statement follows:]

STATEMENT OF STEVEN S. SELTZER, PRESIDENT, MODERN COMMUNICATIONS CORPORATION

Mr. Chairman, Members of the Subcommittee. Thank you for this opportunity to appear before you this morning.

My name is Steven S. Seltzer. I am President of Modern Communications Corporation, a family-owned and operated business that provides radio telephone and paging services to more than 3,000 customers in Pennsylvania, Maryland, and West Virginia. Modern Communications is headquartered in Altoona, Pennsylvania and traces its roots back to 1954. We have been in the radio communications business for almost 30 years, and have invested almost $1 million in equipment and systems to serve our customers.

In addittion to running my company, I serve as a member of the Board of Directors of Telocator Network of America, the national trade association representing the mobile telecommunications industry. Teocator's more than 650 members include cellular telephone companies and providers of conventional radio telephone service. I am also the President of RCCs [Radio Common Carriers] of Pennsylvania, Inc., the statewide association of mobile telephone and paging companies. In addition, I have served as President of Mid-Atlantic RCCs, Inc. and I am a member of the West Virginia RCC Association.

Modern Communications welcomes the Subcommittee's decision to take a fresh look at the cellular applications process. We support the continued use of a lottery to award cellular licenses—the use of comparative hearings would unnecessarily delay the grant of those licenses—but ~~we believe~~ that changes to the cellular lottery process are necessary to ensure that rural America obtains the best possible cellular service with the least possible delay.

In particular, we believe that the eligibility standards for non-wireline cellular licenses should recognize that radio common carriers like Modern have acquired substantial expertise in constructing and operating mobile telephone systems. This expertise is readily applicable to the provision of cellular service, which, after all, is really just mobile telephone service using advanced technology.

Unfortunately, the current rules governing eligibility to apply for non-wireline cellular licenses put radio common carriers on the same footing with the thousands of people without prior experience in radio telephone communications—people who were induced to file cellular applications by firms promising "pie in the sky" profits from the sale of cellular construction permits or licenses to established communications companies such as ourselves.

With the odds stacked against us like that, few radio common carriers have been able to enter the cellular business. In fact, Modern did not even apply for cellular licenses in the areas where it now provides conventional mobile service because there really was no chance that we would be able to win the lottery.

We believe that the rules must be changed so to ensure that cellular authorizations in rural areas are awarded to entities that have demonstrated the ability to construct and manage a mobile telephone system and will serve the Communications Act's goal of rapid, efficient service to the public.

Let me briefly describe to you how a conventional radio telephone company like Modern does business, and I think you will immediately see the similarities to cellular mobile telephone communications.

First, we survey our service area to locate the best locations for our fixed transmitters (known as "base stations"). These transmitters must be located at high points in the service area so that they can communicate with mobile telephones in as broad an area as possible. The better the location, the more effective the service.

A radio common carrier, like Modern, that has been in business for any period of time has to be familiar with the terrain of his territory and with other factors (like foliage and weather patterns) that can affect the quality of radio-based communications. If he wants to stay in business, that carrier is going to have to engineer his system to take those factors into account.

This expertise is directly applicable to the construction of a cellular system. The quality of cellular service is directly linked to the licensee's ability to find the best spots for his fixed cellular transmitters and his understanding of geographic and other factors that bear on the strength of the signal he can put out. In fact, most conventional mobile licensees own or have access to the best antenna sites in a rural area—sites that are or will be used for rural cellular service.

Of course, even after a conventional telephone system is up and running, the operator has got to establish a marketing and service capability to get and keep—and expand—his customer base. Like the marketing and service "infrastructure" of a cellular carrier, we must gear our efforts to the needs of salesmen, professionals,

small businesses and other customers "on the go" who depend upon Modern Communications to keep them in touch with their offices and their clients. Our service must be prompt, reliable, and responsive, or we will lose our business to one of the other mobile communications licensees that operate in our area.

No other applicants for cellular licenses except the cellular carriers themselves can legitimately claim to understand the needs of mobile communications customers as well as we do and have the resources and experience to meet those needs.

One of the most important ways we meet the demands of our customers is by constantly upgrading the service we provide. Mobile telephone service today is more than just two-way voice communications between a customer's car and his or her office. From many of our locations, we now offer our customers such services as:

Call Forwarding. A call placed to a mobile telephone will be automatically routed to a telephone number of the customer's choice.

Delayed Call Forwarding. A call placed to a mobile telephone will be forwarded to a pre-designated telephone number if the mobile unit is not answered within fifteen seconds.

Voice Storage. If the mobile telephone customer is unavailable, a caller can leave a detailed message of up to a minute-and-a-half that can be retrieved by the mobile customer up to ten days thereafter. The mobile telephone customer can also reply to messages left by other subscribers to our voice storage service.

Telephone Number Retrieval. A caller who unsuccessfully tries to reach a mobile telphone customer can leave his or her telephone number so that the mobile telephone customer can later return the call.

In addition to these services, we have entered into agreements with mobile telephone companies in other areas of Pennsylvania to make it easier for our customers to obtain service when they are traveling away from home. Most mobile telephone customers can use their telephones to make local calls when they travel outside their carrier's service area. They can also make long distance calls, but often must first contact the mobile telephone operator and charge the call to a credit card.

Through agreements with other carriers, by contrast, we have made it possible for Modern's customers to *direct-dial* local *and long distance* calls in a number of Pennsylvania cities outside of our service area. We are working now to make direct dial service available to our customers in more cities in Pennsylvania and in West Virginia and Maryland as well.

Of particular concern at this hearing is the provision of cellular service to rural areas. Modern Communications specializes in providing mobile telephone service, including the sophisticated ancillary services I just described, to small communities like Clearfield and Lewistown, Pennyslvania and Cumberland, Maryland. (Earlier this month, more than 3,000 people applied for the remaining cellular license in Cumberland under the FCC's current eligibility rules. I would bet that few if any of those applicants know the ins and outs of providing mobile telephone service to the Cumberland area as well as we do. In that flood of applications, however, the chances that we would be selected to build the cellular system and apply our expertise is virtually nil.)

In addition to serving smaller communities, Modern has constructed facilities in rural areas so customers traveling through these areas on major highways have continuous access to mobile telephone service. We regard service to these highway "corridors" as a critical link in our mobile communications network.

Our experience in serving rural communities and providing coverage along highway corridors in rural areas is directly applicable to the cellular context. Like mobile radio licensees, cellular licensees in rural areas will have to be able to meet both kinds of demand. Unlike the customers of the application mills, mobile radio licensees have shown they can do so.

We believe that mobile telephone carriers' experience and our demonstrated commitment to high-quality mobile telephone service has equipped us to offer the first-class cellular service to the public. Some of us, like Modern, are already agents for cellular licensees in our service areas and are gaining direct experience in the cellular business. As long as the eligibility standards for non-wireline applications remain unchanged, however, the public will not reap the benefit of our expertise.

For these reasons, we strongly support Telocator's proposal to limit rural non-wireline cellular eligibility to *qualified* applicants that have demonstrated their willingness and ability to provide two-way mobile communications, and we respectfully urge the Subcommittee to adopt Telocator's proposal.

Contrary to what you might hear from others, Telocator's plan is not a plot to help the "big guys" gain an even bigger share of the cellular industry. Modern is certainly not one of the "big guys." Rather, Telocator's proposal will ensure that only those companies—large and small—with the experience and ability to provide

low cost, high quality service would be able to compete for rural cellular licenses. Congress must act to stop the abuse of the lottery process, and to ensure that rural cellular service will be delivered quickly and efficiently.

Experience has shown that the self-styled "small investors" that make up 99% of the cellular applicant pool get hurt by losing their money in the cellular application pipe dream far more often than they win. Even those few that win, do so at a cost of more expensive and less timely service to rural Americans. Please support legislation that would end this abuse and ensure that rural America get quality cellular service at competitive prices from people who have demonstrated their commitment to service.

Thank you. I would be happy to answer any questions you might have.

Senator INOUYE. Thank you very much.

Some have suggested that only those who are experienced or with a background in cellular telephone systems should participate in the RSAs. I believe it was ten years ago when we first had our two experimental cellular systems, one in Chicago and one in Washington. So one can safely conclude that before then there were no experienced, qualified persons in cellular telephone systems.

Mr. McCaw, when did McCaw Communications get involved in cellular telephone service?

Mr. MCCAW. Well, if I could just step back to give you a little history, I would like to make the distinction between being qualified operators in cellular as opposed to being technically qualified in two-way communications. Prior to our involvement, which actually began in 1980 and 1981, we were licensed common carriers providing two-way telephone service in other markets. So I think it is important that we separate qualifications as to cellular and radio in general, because they are the same principles; only it is a little different technology.

But we actually began in the two-way business in the 1970s and then proceeded from that business into the logical next step, which was cellular telephone.

Senator INOUYE. Mr. Neff, you are a successful non-wireline operator in Billings.

How long have you been in that business now?

Mr. NEFF. In the cellular business?

Senator INOUYE. Yes.

Mr. NEFF. Off and on since about early 1983.

Senator INOUYE. And before then, were you involved in the telephone business?

Mr. NEFF. I was a commercial deep sea diver for oil and gas companies.

Senator INOUYE. How many subscribers do you have in your system?

Mr. NEFF. A little over 50. We are still in the testing phase. I am going to file a 489 to go into commercial operation within the next two weeks.

Senator INOUYE. Of the number of applicants in the MSAs, how many are presently operating systems, I mean, the successful lottery winners, how many are operating systems now?

Mr. MCCAW. Mr. Chairman, are you addressing me on that?

Senator INOUYE. Yes.

Mr. McCaw. Our information shows that six of the lottery winners have constructed their systems, six out of the 180 that were granted by the lottery process.

Senator Inouye. What happened to the other 174?

Mr. McCaw. Well, the vast majority of those sold out to operators, and there are a few that are still under investigation by FCC and the DOJ. But the vast majority sold their licenses.

Senator Inouye. The other question that has been brought up in this discussion is the difficulty that a subscriber might have in going from the MSA to the RSA, assuming that the MSA system is not compatible with the RSA system, they are two separate systems. So if I have a phone that operates in an MSA and I am driving along and I get into the RSA area, what happens to me?

Mr. McCaw. Again, are you addressing that question to me?

Senator Inouye. Anyone here.

Mr. McCaw. That is actually one of the main concerns that we have. In many cases the Regional Bell Operating Company is operating a regional system, and he is able to offer uninterrupted cellular telephone calls over large areas.

If we have an MSA and do not own the adjacent RSA or there is not compatible equipment, as the person moves from the MSA into the RSA, his telephone call will be terminated. He then will be required to be reverified and replace the call on the adjacent system, so that we cannot effectively compete with the Bell Operating Companies in a business where there is little to distinguish the two.

Senator Inouye. Any others?

Mr. Neff. Mr. Chairman, I disagree with what Mr. McCaw said. In the industry, it is called, the term of roaming, and if I drive, if my carrier in Billings has an agreement with Cleveland, Ohio, if the company is CCI, I could drive my car from one city to the next to the next to the next, and if I was an RSA operator in the State of Ohio, it would have automatic handoff if we had a roaming agreement. It is about .4 second. You do not even hear a beep.

Mr. Henry. Mr. Chairman, I did not want to interrupt the process of your questions. I just want to make a comment on what Mr. McCaw said about the number of folks who are operating the systems.

I do not have enough statistical information to know whether his number of six is correct. I do understand, however, that a lot of those sales occurred after the FCC decided that these construction permits could be sold off.

I think that there is no question, in my mind, at least, that the FCC's decision fueled the speculative fire, if you will, when they decided that construction permits could be sold for a profit.

As I understand the law, prior to that decision, notwithstanding what the Commission said in that decision, the general law was that you cannot sell a bare construction permit for a profit. And the cases cited in that decision I really take issue with as sustaining what the Commission decided there.

So it was a combination. It was not only that there were some speculators in the business. There is no doubt in my mind, at least, that there were some. But it was greatly fueled by that FCC decision.

It was also added to in considerable measure after that decision in particular by folks like Mr. McCaw who would come around and offer prices, I think, that were never contemplated when the folks filed their original applications.

I believe the prices that Mr. McCaw has been paying were never really envisaged when the folks filed their applications in the first place.

Senator INOUYE. Am I to conclude from your statement that you would favor legislation that would prohibit the sale of construction permits for profit?

Mr. HENRY. Well, what I have said in my testimony, and what we do favor, is just that. Enforcing the law as we see it, which would prohibit the sale of construction permits, bare construction permits for a profit.

Now, we are not certain that legislation is needed. We think it is the law.

Mr. NEFF. I agree.

Senator INOUYE. Mr. Seltzer.

Mr. SELTZER. Certainly the FCC's change in position has added fuel to the fire, in my opinion. It has certainly increased the opportunity for speculators to get into this and make what I would term a "quick kill."

Notwithstanding this change in position, we have seen particular, where we come from, central Pennsylvania, a company build a system, a turnkey system for the licensee, and then buy that system back from the licensee after construction.

It makes it slightly more difficult, but nonetheless profitable for a speculator to build the system. He is going to be a winner no matter how it happens. Whether he sells a constructed station or he constructs it, he is going to get his money many times over.

Senator INOUYE. Mr. McCaw.

Mr. MCCAW. I would make two comments on that. The first would be that I would be concerned that there would be an incentive for the person being granted the license to construct inexpensive throwaway cellular equipment.

He would put up something very inexpensive, get his licenses, and turn around and try to sell it to the adjacent operator. Now, that creates two problems. Number one, it has increased our cost of trying to buy the license and to provide service into the area, because the capital cost of equipment has already been incurred.

And number two, in the meantime, our competitor, the Bell operating companies, the wireline side, will have a head start. They will be operating with a system that would be totally compatible, with adjacent metropolitan areas, offering handoff where our system could not.

So again, in an industry where there is little to differentiate between two service providers, I would be concerned that we would lose customers in the existing MSAs, because our competitor could say that they could provide service that we could not.

Senator INOUYE. Senator Packwood.

Senator PACKWOOD. Mr. McCaw, when you got into this business, you knew what the rules were at the start, including the wireline set aside.

I wonder if it is fair to come and complain afterwards, when you got into it knowing that?

Mr. McCaw. You know we are not here to complain, Senator. I think our position is that we only want equal footing.

And if the original intent of the Congress was to provide two economically viable, competitive carriers, I think that is all we are asking today, that we be allowed to compete on an equal footing with the wireline side.

We are certainly asking for no special favors. We are asking actually for less than they already have.

Senator Packwood. Would the non-wired franchises, if sold, go for more than the wired franchises? Would it reflect a difference in the capacities of the systems?

Mr. McCaw. I am sorry. I am not sure I understand the question.

Senator Packwood. I am curious if a non-wired franchise in a metropolitan area is worth less than a wired franchise?

Mr. McCaw. Sales have shown that they are worth roughly the same amount.

Senator Packwood. Worth what?

Mr. McCaw. Roughly the same amount.

Senator Packwood. Why is that if the wires have an advantage?

Mr. McCaw. Well, there have been few wirelines ever sold. So it is really hard to make a direct comparison.

But today, the head start issue in the MSAs is over. I would say that there would be a discrepancy in the future if one license were viewed to be less economically viable than the other.

Senator Packwood. But at the moment, you are saying, in terms of the MSAs, they are viewed as roughly equivalent value?

Mr. McCaw. Roughly equivalent.

Senator Packwood. Now, Mr. Henry, in your testimony, you talk about the lottery winner and you say, an applicant must provide additional evidence of his basic qualifications. This is after the applicant has won the lottery, I guess.

If the FCC is not satisfied with those qualifications, either through its own analysis or through a filing by a third party, apparently they can turn down the application. Is that right?

Mr. Henry. Yes.

Senator Packwood. Am I free to say that your testimony indicates then that no speculator who is unqualified has gotten through this process to the end and received a license?

Mr. Henry. No, sir. I am not saying that. I am saying that they have found that, well, there are a number of reasons for that, I think, as was indicated in the testimony of the FCC.

Initially, they did carefully screen the applications prior to the conduct of the lottery. And their testimony was that they felt this did eliminate a number of the speculators, and I would not disagree with that.

They then said that that took so long that they decided to screen only the financial and legal and technical qualifications of the winner of the lottery. And they do do that.

I think it is very difficult, just from a bare analysis of legal, technical, and financial qualifications, to determine whether a person is a speculator or not, because that is a matter of intent, and the FCC has so acknowledged.

But as far as our members are concerned, whom I emphasize are potential applicants, that is a perfectly proper process to determine that they are fully qualified under the terms of the law.

Senator PACKWOOD. I do not understand what your statement means. When it says "each applicant has been required to submit an application containing an extensive amount of engineering data about system construction operation. Upon being selected as the lottery winner, an applicant must provide additional evidence of its basic qualifications."

If they do not, apparently they are turned down even if they won.

Mr. HENRY. That is right.

Senator PACKWOOD. The basic qualification is whether you have any ability to run the system. Is that not something the FCC is concerned with or looks at?

Mr. HENRY. Well, I think they are because they have established financial qualifications, at least to their satisfaction. So that is a very important factor.

They have determined that the system, as proposed, is capable of carrying out its mission to provide service, and that the applicant is legally qualified to carry it out. They do not require that you have been in the business before, however.

Senator PACKWOOD. Mr. Neff.

Mr. NEFF. As we are all aware, this is a very young infant industry.

Senator PACKWOOD. A very what?

Mr. NEFF. A very young industry. And with respect to most new businesses, it takes a growing period to learn how to operate it efficiently.

I have made plenty of mistakes in the past, and I will continue to do so. But hopefully not to the scale I did. I think Mr. McCaw can attest to the fact that it takes an extreme amount of work to operate a cellular system.

But the point that I am trying to make is, with respect to who is actually qualified today to operate a cellular system, I do not believe that I am more qualified than anyone in this room.

Senator PACKWOOD. Thank you, Mr. Chairman.

Senator INOUYE. Senator Adams?

Senator ADAMS. Thank you, Mr. Chairman. First, Mr. McCaw, the members from the FCC and FTC said they did not know, or could not give us figures as to how much the consumer was having to pay for this speculation.

Can you tell me what was the disposition in the non-wireline markets that primarily impacted on this speculation? In other words, how many were sold or not sold, and how many were up for sale in, say, the 120 to 305 market, which has been one of the most recent?

Mr. MCCAW. Well, as I stated earlier, our information showed that only six of those 180 markets granted by lottery had been built by independent operators.

Of the rest of the 180, we showed that in excess of 110 were sold or are under option to be sold, 34 are for sale, and we have approximately a dozen that are currently under investigation by the FCC to determine if the original applicant was qualified.

Senator ADAMS. Let us get to the point of this, which is that we have got the wire systems out there, and we have set up a system where there is to be competition by the cellular system, which nobody has really explained yet, but it is simply a handoff of the digital system from cell to cell to cell, as you go throughout an area.

Now, that means you have got to handoff from an MSA to an RSA or thereabouts in order to make it viable. How much did you pay for these? In other words, how much did the consumer, and we will just take your example because we do not have what other people have done.

How much did you have to pay these people in order to get this handoff from one system to another, and to get into these MSA lottery winners? What did you pay them?

Mr. MCCAW. I do not have the exact figures in front of me, Senator. But I can say that the figure would be in the tens of millions and maybe as high as into the hundreds of millions.

Senator ADAMS. In other words, you paid $100 million, which obviously the consumers or somebody is going to have to pay for people who got something for nothing. So you have paid out $100 million.

Mr. MCCAW. That is a fair statement, and that was one of our original concerns going into the RSA lottery, in that we be protected from having to operate from a much higher capital cost than our competitor.

Senator ADAMS. That was going to be my next question. If the wireline gets it automatically, as Senator Packwood pointed out, then the others have gotten it for zero. And you have to buy these people out to make this cellular system work.

And I am going to turn to Mr. Neff in a moment on stand alone systems as compared to wire systems. You have got $100 million competitive disadvantage to start with. Have you not?

Mr. MCCAW. Yes, and actually, Senator, that is only part of the problem. Again, I want to reiterate the concerns we have as to delays and us providing service vis-a-vis our competitor.

I am concerned about the ability to handoff between MSAs and RSAs, which I have to disagree with Mr. Neff on in that I think he is confusing handoff with roaming. Handoff implies that you have compatible equipment, whereby the switch will automatically hand from one cell to the next, and not drop the call. Roaming does not include that service.

There is another important point to be talked about here, I think, and that is that there really has been somewhat of a changed circumstance between when the original lotteries were held and the industry as it exists today.

There has been a trend toward the development of regional systems. And I will grant you that in the earlier rounds of the lottery, many people intended originally to build systems. I think there were a lot of people who wanted to.

The fact of the matter is that economically, many in those MSAs, they could not compete. And if we take that one step further into the adjacent RSAs, the economics are very, very poor.

Without the ability and the economies of scale of operating in an adjacent system, I am not sure that you will end up with two sys-

82-856 0 - 88 - 3

tems in those RSAs. You might well end up with a monopoly wireline system.

Senator ADAMS. Mr. Henry, I want to turn to something here because I am concerned about it. How long ago was your association formed?

Mr. HENRY. The association was formed in the late fall of 1987.

Senator ADAMS. In other words, about two or three months ago?

Mr. HENRY. Yes. It was formed very soon after Mr. McCaw came up on the Hill to try to get his proposition across in the House of Representatives.

Senator ADAMS. Are you an officer or director of the association? Or are you just counsel, or what?

Mr. HENRY. Just counsel.

Senator ADAMS. You have an executive director?

Mr. HENRY. We do.

Senator ADAMS. Who is that?

Mr. HENRY. Eleanor Calamari.

Senator ADAMS. What I am concerned about is I got a copy of your newsletter, and Mrs. Calamari, is that how you pronounce it?

Mr. HENRY. Yes.

Senator ADAMS. Says in this that she met with me and that I said, "you made your point." And that she met with my staff.

Now, the only time that she has ever met with my staff was on November 25th, and I was out of the country, and I have never dealt with this woman. Now, what is this all about? Why did she do that?

Mr. HENRY. I cannot say why Mrs. Calamari said something that may not have been true. I assume it was a mistake. She did meet, as I understand it, with your staff.

Senator ADAMS. Oh, sure. We meet with everybody. But I have never been involved with this, and that kind of hits me a little wrong that I am quoted and it is sent around the country, when I have never seen the woman.

Mr. HENRY. Well, I would have to look at that myself.

Senator ADAMS. I will give you the copy if somebody will take it down, and I will not pursue it any further. But I am surprised.

Mr. HENRY. Well, Senator, if your question essentially goes to the bona fides of the association, I think there has been talk about the fact that it is newly-formed, et cetera, and that it is an association of members who have been asked to join. It is.

But I can assure you that it is a bona fide organization, and it has a five person board of directors that are quite qualified.

Senator ADAMS. Well, I am not going to pursue that any further, Mr. Henry. You can look at it and we will talk about it later.

But the point is this, that what the Committee is interested in is, we have got a lottery system here which has sort of blown out of control 97,000 applications, and now 200,000.

And what the Chairman has indicated, and I think we are trying to go with it, we are trying to correct a flawed system and provide quality service and a competitor to existing wirelines who are going to have this.

And they are in regions, I am very familiar, as I know Senator Packwood and the Chairman is, with the Bell operating companies.

They are regional, there are only seven of them. They cover these areas, and can go with compatible systems.

And Mr. Neff, what my concern is, is you have got a small system and I wish you well and so on, but when you start talking about competing in a rural area with an existing company and having off in a digital system where you have got to go from city to city to city, your stand alone cellular system out there against that wire system, without some kind of way to tie into the other cellular systems, is going to mean that you have got not only an inferior system, you are late coming on line.

And if everybody else around you in the non-wire system has paid, and I do not know how much you are going to pay for 200,000 applications as opposed to 97,000, in other words this market is obviously growing, a great capital disadvantage.

What we are interested in is seeing that we get quality service out there. And I am surprised that you, and you state in your statement that you would join and endorse what Mr. McCaw said, which was kind of a double lottery, because you would benefit from it personally, but you are against it because you want everybody to come in.

I just do not see how that follows. It seems to me that what you are interested in, what we are all interested in, is creating this cellular system that is compatible as soon as possible to compete against the wire system, and that we ought to have a way to do that without spending several hundred million dollars in buying out speculators.

I just do not understand why you have not joined with everybody else. We could have a consensus suggestion of how to get a lottery. And what Mr. McCaw suggested is one. And I think it is a good one.

I do not like the bare bones construction permit system, because I have been in the transportation business and telecommunications business operation, and you know, you can get a turnkey and it is non-compatible. And then you peddle it.

It just seems to me we want to have a system that in some way goes to what a cellular system is. Which is a handoff system cell-to-cell. And we want to get it in the rural areas where there are few people.

So it would seem to me that you would want to join in this effort to get this service. Go ahead. The wire services are going to be out there anyway.

Mr. NEFF. Senator Adams, for the record, Mr. McCaw was correct with my terminology between roaming and handoff. It is my opinion that well in excess of 50 percent of the RSAs are much more viable stand alone systems than a lot of the lower-tiered markets like the one I am in.

I can assure you that I could build a system, an RSA in the middle of a state that I do not live in that is surrounded by one or two companies, if it was one company owning the whole thing, and I will give you a for instance.

Senator ADAMS. And face the BOC?

Mr. NEFF. And compete competitively against the wireline. There is no doubt in my mind.

Senator ADAMS. Mr. McCaw, what do you say to that?

Mr. McCaw. Well, first of all, I think that Mr. Neff has done a good job building his system in Billings, Montana. I think it is still to be determined, however, if that system is going to be economically viable.

He is not competing against a Bell operating company, but rather an independent telephone company. And I am sorry I cannot tell you which one. But it is an independent rather than a BOC.

I would suggest to you that Billings is the exception rather than the rule in this country, because it is not representative of an area where a regional system is mandatory to remain competitive.

So I disagree with the concept that you can compete with a regional system if the RSA that you are granted, or that you win, is in an area that is competing with a regional Bell operating company.

Senator Adams. All right. Describe to me, let us take the area that I know, where you have got the Seattle regional area, but then you have got this broad rural area.

I am not going to compare it in size with Senator Stevens' State of Alaska, but just describe to me how you are going to work this system, if the RSAs are not tied together in some way, and you have got a very strong operating wireline operation in the area?

I think we need to hear that, because there is some reason that you are paying a lot of money and I assume others are paying a lot of money to get this system. So describe to me what is going to happen out there.

Mr. McCaw. First of all, we have only paid for markets that we need to fill in pieces. If you look at the State of Washington, it resembles a jigsaw puzzle as to how it is divided between MSA and RSA.

And in many cases we own MSAs with an RSA on either side. Or we own two MSAs with an RSA in between. In many cases, there are interstate highways that run right through the MSAs and RSAs. So we end up with an MSA, then a blank, then an MSA, then a blank, and then an MSA.

The regional Bell operating company in that area owns everything from the Canadian border to the border of Oregon running on Interstate 5. We own the only MSAs there. If there is an incompatible system anywhere along there, we are at a severe disadvantage.

Senator Adams. What happens is you get a cutoff, do you not?

Mr. McCaw. You get a cutoff. You are not able to continue your call. You have to replace the call.

Senator Adams. So if you are driving, let us just talk about the basics because I think that the Committee is trying to produce quality service for rural areas.

If you are driving out of the MSA in Seattle, and you hit an RSA, and it is either owned by a speculator, or I do not care who owns it, but anyway it is not compatible, what happens to your telephone call in your car?

Mr. McCaw. Well, obviously, the call is terminated, and they must replace the call again.

Senator Adams. So you are out advertising a system saying, we will handle you in this city and we will handle you in that city.

And Mr. Neff said, you know, he had an agreement with somebody in Cleveland, but we are talking about in a state, if I am going to go buy one of your systems, I want to go across the State of Washington and use it. And the other side that is already there and has a monopoly produces that, do they not?

Mr. McCaw. That is correct.

Senator Adams. So you have got to buy the middle system, do you not?

Mr. McCaw. If we do not buy it, we have no control over the technical quality of system, the rates, and many other aspects of service.

So, in other words, the guy in the middle can charge double our rates, and every one of our customers can roam onto that system automatically on the A wire, and we would not be able to compete. And he might have to charge excessive rates to realize any kind of rate of return on his system.

Senator Adams. That is what I was going to ask Mr. Seltzer, because he has been in this business.

And it is what we used to call in the telecommunications business, Mr. Henry, the windshield areas, which meant that you had to go out and repair the lines in individual cars, and you had the rain on the windshield.

Now, Mr. Seltzer——

Mr. McCaw. Excuse me, Senator. I would just like to make one more statement, just to maybe clarify something Mr. Neff said. And that is that we have not asked for any eligibility preference in areas where we do not have two adjacent MSAs to the RSA.

And I think that is very important to note. I mean, he might be under the assumption that we have asked for some kind of preferential treatment for all the RSAs. We have not asked for it where there is no adjacent MSA, we have not asked for any preference where there is one adjacent MSA. Only where there are two adjacent MSAs.

Senator Adams. So you are trying——

Mr. McCaw. What we are saying is we are only asking for those where we feel it is actually a regional cellular system, because if we look at the way these areas are divided up the divisions are geographic, and they are not necessarily marketplace.

So you divide it by means of census rather than what the natural marketplace is. And it creates a very artificial representation of the areas we are trying to serve.

Senator Adams. Mr. Seltzer, do you have a comment? I have not let you comment in my question period. Whatever you want to say.

Mr. Seltzer. Mr. Adams, I feel somewhat uniquely qualified to talk about rural service areas because I was born and raised there, and I live in what I would call rural America today.

The areas that our company serves are basically portions of four RSAs, and I feel very strongly about the importance of customers that we would sell, whether we are an agent or whether we are the licensee.

I feel strongly about the importance of customers being able to use what is now being termed as a super-system concept, where they can go from an RSA to an MSA or vice versa, without calls

dropping, without having to place the call again, without incurring roaming charges, which are relatively significant.

When you start talking about rural America, and you are going to tell a gentleman who lives for instance in Altoona, Pennsylvania that he is going to go to State College, which is a 40-mile drive, and he is going to pay $1.65 for every call and 60 cents a minute because he is a roamer, I feel that economically the public is hurt.

The super-system concept, which is really what you are starting to talk about here, you are talking about an RSA between two MSAs, or adjacent to an MSA, I think it is critical for the cellular operators.

We are not one, but I can tell you because I live there and I work there that it is important that it is compatible, that the calls do not drop, that the control is maintained, that the quality of service is what we want it to be.

Senator ADAMS. Thank you, Mr. Seltzer. Thank you, Mr. Chairman.

Senator INOUYE. Mr. Henry.

Mr. HENRY. I would just like to comment, if I may, on some of the questions and answers that Senator Adams got, because I think the record would be incomplete without them.

And speaking of completeness of record, Senator Adams, I have now seen this newsletter. This is not put out by my client. This is another organization. They do quote Mrs. Calamari, but it is not our organization that put it out. I just wanted to get that in the record, if I may.

On the question of handoffs, and Mr. McCaw's inability to have his customers pass through these RSAs and be handed off, if those RSAs are in the hands of other people, what my clients tell me is that is simply not the fact.

It is in both companies' best interests to have handoff agreements, because if somebody from Seattle, and I do not know my geography in Washington State so forgive me if I am a little off.

But if you are in Seattle and you want to go south through an RSA, and the Seattle area is Mr. McCaw's, and you want to go south through an independently-owned RSA and then into an MSA down south that is owned by Mr. McCaw, it is in Mr. McCaw's best interest if that RSA is awarded to an independent operator to have a handoff agreement.

All he has to do is have an agreement, because he does not want his customers to say that if they are going to go, once it is a fact that the independent is in there, Mr. McCaw does not want his customers to say, look, I am sorry, I cannot, if you go through this rural service area, they got it all screwed up in Washington but there is nothing I can do about it. He is not going to say that.

He is going to say, I will go make an agreement with the independent, and we will have a handoff agreement. Because it is in his best interest to do so, as well as the best interest of the independent to do so.

Now, the question is raised about whether the equipment of the independent operator is compatible. But again, since there is every business incentive to make these handoff agreements, then there is every business incentive for the independent, if he or she gets in, to

buy compatible equipment with Mr. McCaw's MSAs that surround it.

So I guess in a nutshell what I am saying is I think Mr. McCaw does not have to pay extra, if you will, in order to have handoff agreements. He will get them in the due course of normal business.

Senator ADAMS. Oh, but you have got already out there a Bell wire system that is very competitive and so on. And there is not any bargaining in that situation that you outlined.

They are going to ask for him to pay for the equipment, pay for the license, pay for everything else imaginable. It is obvious that is where the speculation is coming from, that is where the $200 million or $300 million come from. And he has got to get into the field soon, because he has already got a monopoly against him.

And so what we are trying to do is get this compatible system, and not just run up the cost, because buying out or going into these agreements without some kind of government regulation over it, and the FCC and the FTC have testified they cannot handle it, if we do not have this thing set up in a different way then whoever is in the middle of this thing just charges, and that goes to the customer.

And it is rates, as Mr. Seltzer managed, or it is a payoff by the company coming in. And so I just simply, Mr. Henry, I understand your position. If I was sitting in the middle between RSAs, I would like it too. But it is not a very good thing when we have already got a monopoly in the field.

Mr. Chairman, I did not intend to take that long, and I know there is a vote on. So whatever is your pleasure.

Senator INOUYE. Thank you very much. The letter dated January 22nd from the Honolulu Cellular Telephone Company will be made a part of the record at this time.

The Committee will stand at recess for 10 minutes. And when we reconvene, panel number three, consisting of Mr. Maher, Mr. McAllister, Mr. Stroup, and Mr. Blum will be on deck.

[Recess.]

Senator INOUYE. Our third panel consists of Mr. Robert Maher, President, Cellular Telecommunications Industry Association, Mr. John McAllister, President, West Carolina Rural Telephone Cooperative, Thomas A. Stroup, Vice President, Telocator Network of America, and Mr. Thomas Blum, General Manager External Affairs, Bell Atlantic Mobile Systems, Inc. Mr. Maher?

STATEMENT OF ROBERT MAHER, PRESIDENT, CELLULAR TELECOMMUNICATIONS INDUSTRY ASSOCIATION

Mr. MAHER. Thank you, Mr. Chairman. I am Bob Maher, President of CTIA, which is a three-year old trade organization representing more than 93 percent of all the cellular licensees building in the top 90 markets.

These are wireline and non-wireline carriers, in addition to manufacturers and other associated with the industry. I would like to just summarize my testimony and include it for the record, if you will.

I think it is pretty well agreed that cellular service has seen an unparalleled acceptance by the public. We are putting subscribers

on at a rate of about 35,000 a month. And I think that will increase.

We had our millionth cellular subscriber sign on last October. This also evidences the public desire to subscribe to cellular, and its importance to our business community.

We are almost ready to open cellular service in the 200th city, which means that 70 percent of the Nation's population has access to cellular. We are ready to proceed as quickly as possible in building the rest of these systems, and in getting into the rural areas of the Nation.

Right now the purpose of the hearing is evident. The cellular industry faces an enormous roadblock. That is the flood of applications that threaten the FCC.

It has been evident that three things have happened, three landmarks, that portended this threat. First, was when we departed comparative hearings, we saw scam artists around the country selling applications by telling an unsuspecting public that they were going to get rich quick.

CTIA wrote in 1984 to the FTC, the Justice Department, the Postmaster General, and because we were getting so many calls, we wrote the Congress. The FTC did move in, but only after literally tens of thousands of applications had been sold.

A company had bilked the public of more than $20 million, and indeed a lot of people were stung by this. I think that should have been a clue to the Federal Communications Commission at the time that something was going astray.

The second thing that they should have paid close attention to was when batches of identical, Xeroxed cookie cutter applications started coming in. Dating back to 1981, the Commission said that this would not be a national lottery.

They used such terms as "insincere applications". They used "speculators," they used "cookie cutters." They even tailored the process so that everyone had to file at the same time, so indeed, an individual could not go in, lift an application, Xerox it and file it.

The first time that the identical batches, and I do mean identical, hit the Commission, that should have been a clue. And they should have, I think, thrown them all out, because in their own regulations, they said that the individuals should have a personal involvement in the preparation of the application. I think that it was obvious they did not.

The third instance contributing to today's situation was when, in December of 1985, the FCC renewed the financial requirement for applicants. CTIA filed in that docket, asked the FCC to reconsider and said at the time:

> Absent the requirement of a financial showing in the initial application, applicants who would not otherwise be qualified may now file in the hopes of being the lottery selectee, at which time they can attempt to qualify themselves by securing financing.

CTIA made the point that this will particularly disadvantage legitimate individuals and corporate non-wireline applicants. It did not take a rocket engineer to know that these application mills had been cranking up for a year and a half, and they were on the threshold of indeed breaking down the whole process, which literally happened.

In previous testimony, witnesses were talking about the scope of this problem financially. To give you an idea, the cellular industry has invested, in four short years, approximately $1.75 billion in capital costs.

It may indeed cost almost that much for legitimate cellular carriers to buy the RSA licenses from speculators if something is not done and the mathematical wizardry of application mills prevails.

The low estimate will run somewhere in the area of $680 million. A more reasonable estimate based on a simple policy of $20 per population will go closer to $1.25 billion. There is no value added there. There is nothing passed on to the consumer or to the industry or to the service, except added debt.

If you just look at, and this was explained earlier, the rapid acceleration in the number of applications, and if anyone took the time to see how the applications had gone up, you will see how speculators have jumped in.

Senator INOUYE. Proceed.

Mr. MAHER. I am sorry. I did not know I was under time constraints here, in which case I will go right to the bottom line.

We are very, very concerned that the FCC really has known about this for some time, and has taken no interest in it. They have not shown the will, to correct abuses. They have changed the rules seven times. At every step they have done so to accommodate the administrative procedures of the FCC and not looked after the legitimate applicant, which in the end means the consumer.

We think that the only way to get back on track in an expeditious manner, which also is of great interest to everyone in the cellular industry, wireline and non-wireline, is to put most of the basic qualifications that we originally required of an applicant, back in.

We favor this because it will not require Congressional legislation, which means we do not have to wait 6 or 8 or 9 or 10 months for the process to finally produce law.

The FCC has the authority to change these without further delay. And I think that the head of the list would be firm financial requirements based on either a generic model or specific individual estimate of how much the system would cost.

The rule of thumb is that an RSA system would be about $1 million to build and operate for one year. It would be like the FCC has done in the mobile satellite case, actually make people put money in the bank to show committment.

There are additional qualifications which are listed in my testimony, again, which are not exclusionary. They are just sound business principles, which are required in every other broadcast and most communication situations where licenses are involved.

I will be glad to answer questions.

[The statement and question and answer follow:]

STATEMENT OF ROBERT W. MAHER, PRESIDENT, CELLULAR TELECOMMUNICATIONS INDUSTRY ASSOCIATION

Mr. Chairman, Members of the Committee, I am Bob Maher, President of the Cellular Telecommunications Industry Association. CTIA is a three-year old trade association representing more than 90 percent of all cellular licensees, both wireline and non-wireline, in addition to nearly all the major manufacturers and those other sectors affiliated with the cellular industry.

The commercial cellular industry was born just a little more than four years ago. Since then, its growth has been almost unparallelled in subscriber acceptance despite protracted administrative and regulatory delays. Last October, the one millionth cellular subscriber was signed on. We are signing up new subscribers at a rate of more than 35,000 per month. This record is a source of great pride to members of the cellular community. But, more important, it evidences the value of cellular service and the public's desire to subscribe to it.

We now offer cellular service to people in 200 cities, making cellular available to 70 percent of the nation's population. We are ready and anxious to extend cellular service to rural areas where it would benefit both rural residents and urban residents who travel to or through rural areas. Unfortunately, a very large regulatory obstacle threatens to delay extension of our services. The obstacle results from the FCC's well-intentioned but unsuccesful efforts to expedite the cellular licensing process and from the appearance of consulting businesses which capitalized on the FCC's efforts by mass producing cellular applications and mass marketing them as though they were tickets in a state-run lottery. The consequence has been great for these "application mills," but bad for the vast number of individuals who bought the mills' cellular applications thinking they had aspects of an investment rather than a wager, bad for CTIA's members who are ready and able to provide service, and disastrous for would-be non-wireline cellular subscribers anxious for an early opportunity to obtain service.

Let me give you an idea of the extent of the problem. To date, capital investment by cellular operators is about $1.75 billion. This figure represents the millions of dollars spent on cells, switches, offices, equipment and operating personnel to build and operate systems.

Yet if something is not done to correct the rampant speculation which has plagued the industry for the past three years, nearly as much will be spent just to purchase licenses from these speculators. A conservative estimate may be as low as three-quarters of a billion dollars with a more realistic estimate coming in at a billion and a quarter dollars. That money will be spent for piece of paper, not for equipment or personnel.

More important, I predict that if something is not done to end speculation, many rural service areas will not be served by non-wireline companies for two or three years, if ever.

I think there is a consensus that the FCC's process to award non-wireline cellular licenses has broken down. This breakdown can, for the most part, be traced to two related causes. First, national scam application mills took advantage of the FCC's adoption of lottery procedures to hit the media with get rich quick ads, promising that nearly all buyers would become millionaires. The advertising in national media was misleading on its face and CTIA wrote to the FCC, the Federal Trade Commission, the Department of Justice and the Postmaster General asking that they investigate. Only the FTC tracked the case and, in the end, closed down the largest application mill after it had taken in more than $20 million for applications. Of those applications filed with the FCC, to my knowledge, none was rejected. This should have been the first warning that the process was defective in weeding out speculators, or insincere applications, as the FCC termed them in its warnings. But the FCC did not follow these warnings with action and speculation grew.

The second significant factor was the FCC's December, 1985 decision to remove proof of financial ability as an application requirement. CTIA petitioned the FCC to reconsider its Order, stating:

CTIA is additionally concerned that by modifying its rules to eliminate the financial showing requirement, the Commission may not further its goal of discouraging frivolous applications or speculation in cellular licenses. Absent a requirement of a financial showing in the initial application, applicants who would not otherwise be qualified may now file in the hopes of being the lottery selectee, at which time they can attempt to "qualify" themselves by securig financing. This will particularly disadvantage legitimate individual and corporate non-wireline applicants.

CTIA's predictions that legitimate cellular applicants would be mathematically overwhelmed by speculators have been realized. Before the lottery was adopted the Commission received 1,110 applications for the top 90 markets, or an average of 12-13 applications per market. After the lottery was adopted, but before the financial qualifications requirements was eliminated, the Commission received 5,182 applications for the next 30 markets, or approximately 173 applications per market. In the six months after the Commission eliminated the financial qualification requirement the Commission received almost 93,000 applications for the next 185 markets, averaging over 500 applications per market.

The fact that plainly unqualified persons—those without any ability or inclination to build and operate a cellular system—now hold cellular licensees should cause concern to anyone desiring to see the public receive service. The fact that 80 percent of the licenses issued between markets 121 and 305 have been sold or are for sale should speak to the sincerity—to use the FCC's word—of those licensees.

The public interest problem that flows from this dismal story is significant delay in the availabilty of non-wireline cellular service. Delay is inherent in the virtually inevitable transfer of cellular licenses from speculators to operators. Delay hurts prospective cellular consumers by depriving them of an increasingly important service. Delay impairs the FCC's fundamental policy favoring the competitive offering of cellular service. And delay hurts CTIS's membership by reducing aggregate demand for cellular service. The only interest truly benefiting from the present approach to licensing is the application mills.

We now face the second phase of the application process, the awarding of Rural Service Areas licenses. Best estimates are that more than 100,000 applications will be filed if something does not change. Last week two "wild card" MSA licenses were opened and nearly 3,200 applications were filed. While it may not be entirely fair to extrapolate from this data to the Rural Service Areas, such extrapolation would indicate that the Commission could receive over one half million applications for the rural areas. In any event, last week's filings certainly give a clue of what is to come.

CTIA has concluded that the most effective way to ensure that speculative applications do not cause massive delays in initiating cellular service in rural areas is to require all new applicants to show that they are ready, willing and able to construct the systems for which they have applied. In order to do this the Commission ought to reimpose financial qualification requirements on all new non-wireline cellular applications.

Historically, the Commission has required applicants for any radio license to show that they have the financial ability to construct and operate the proposed facilities. Financial requirements were initially included in the cellular rules. It has only been in the past few years that the Commission has decided that demonstrated financial qualification at the application stage is unnecessary. It is clear that in this case the "experiment" has not worked. Elimination of the requirement has not expedited the award of licenses. Rather, it has crushed the FCC's administrative apparatus with speculative filings. CTIA suggests that the most effective way to speed the rural licensing process and to weed out speculative applications would be to require all new non-wireline cellular applicants to demonstrate their financial qualifications either by:

(1) Placing in an escrow account one-third of all system equipment costs and the costs of all operations for one year, or

(2) Obtaining a letter of credit for those costs.

The amount to be placed in an escrow account or for which a letter of credit would be obtained could be based either upon a detailed cost submission contained in each application or upon a generic cost estimate generated by the Commission.

There are many advantages to the reimposition of true financial qualification requirements, demonstrated at the application phase. First, of course, the requirement would discourage frivolous applications. This would speed service to the public by vastly increasing the probability that the lottery selectee is ready, willing and able to construct and operate a cellular system. Second, the rule changes could be accomplished by the Commission without Congressional action enlarging the FCC's authority. Third, it would not increase the present administrative burden on the Commission staff in any way. The Commission presently is obligated by the Communications Act to establish the basic qualifications of each licensee—this proposal only affects the timing of the demonstration of financial ability. Finally, the reimposition of a requirement of financial qualification for all new applicants would not impose an undue burden on a serious applicant.

There are other alterations which also would improve the FCC's licensing process. In the interests of time, I will merely mention them. I would, of course, be happy to elaborate upon them. The improvements include:

Require every RSA Applicant to be a corporation or partnership qualified to do business in the state in which its cellular system will be located.

Require every non-wireline RSA applicant to subscribe to a notarized statement reciting participation in preparation of the application and verifying its intention to operate.

Require every new non-wireline RSA applicant to list the principals of the applicant and the management and technical personnel who will operate the system.

Require every new non-wireline RSA applicant to supply a business adress and telephone number.

Require every new non-wireline applicant to supply operational data signifying its intention to operate.

Prohibit any non-wireline applicant from having an ownership interest in more than one application for the same RSA.

Prohibit any party from taking an interest of any type in more than one non-wireline RSA applicant that is contingent on the successful award of a construction permit or license to that applicant.

I appreciate this opportunity to express CTIA's views. Thank you.

QUESTION OF SENATOR PRESSLER AND THE ANSWER

Question. Do you have any alternative proposals for limiting speculation without eliminating serious competitors or putting undue burdens upon their involvement?

Answer. CTIA believes there are several steps which can easily be taken to reduce purely speculative filings without imposing undue burdens on qualified candidates. These suggestions correspond with the original intent expressed by the Congress and the FCC when the lottery system replaced comparative hearings as a method of selecting licensees. The basic premise was and is that applications should be qualified to build and operate a cellular telephone system in order to enter the lottery.

Financial qualifications are the most visible, the most susceptible to objective verification, and probably the most important of the basic qualifications. Originally, the cellular rules required that an applicant be financially qualified to build and operate a system for one year. We think that this is still a valid measure for applying.

The FCC has just proposed the reinstatement of a financial showing at the time the application is filed. We think that is an excellent proposal. We were very pleased to see it accompanied by certain very useful additional requirements designed to limit evasion where an applicant relies upon outside fnancing to establish its qualifications. Specifically, we believe proof that a lender has examined the applicant's financial condition and has established its creditworthiness and disclosure of material conditions for maintaining the financing commitment in force—all of which the Commission has proposed—are quite useful.

We believe certain additional requirements would help perfect the Commission's program. For example, an applicant relying on outside financing should be allowed to demonstrate its ability only with a firm financial commitment from (a) an institution, the deposits of which are insured by a federal agency, or (b) a federal or state chartered bank, savings and loan association or other depository institution. Limiting the source of third party funding to depository institutions would avoid the experience of the past when application mills simply provided dubious "financial commitment" forms supported by a "Dear Applicant" photocopy that was used in hundreds or even thousands of separate applications.

Other financial institutions such as insurace companies and investment banks also could play a part by serving as guarantors of commitments by depository institutions. However, the FCC should require each loan guarantor to be identified and the terms and conditions of the guaranty to be disclosed to insure that it is legitimate. To prevent circumvention, the Commission should permit only established financial institutions to guarantee loans.

CTIA also feels that the FCC should require (a) the loan commitment to be legally enforceable and (b) that it be evidenced by a sealed attestation by the applicant and by the lending institution (1) that a credit agreement exists, (2) that the borrower is not in breach of the agreement, (3) that no funds have been drawn against the agreement, and (4) that the financial institution is obligated to extend the credit to the borrower on demand through a date certain.

CTIA also believes that certain other routine requirements—well established in other sectors of business and industry—would be useful. For instance, the FCC should require that the applicant be a corporation or partnership registered to do business in the state where the applicant is filing for an RSA license. Logic indicates that if the applicant wants to run a system in a state, that person must eventually be licensed to do business there. We know of no situation where a state, local or federal government agency would allow bids or contracts to be accepted for consideration if the applicant were not registered to do business. The cost of this would be minimal.

Should these suggestions not eliminate speculation completely, this type of requirement would have an additional benefit: it would insure that the applicant has at least some involvement with the application. In the recent past, despite earlier FCC requirements that the applicant have a "personal involvement" in the prepara-

tion of the application, the individual speculator simply has signed off on a form that a cellular consulting firm has prepared and mass marketed.

This raises a very important point. The effects of tens of thousands of speculative applications on the cellular process obviously is a serious problem requiring the attention of both Congress and the FCC. The immediate cause of the problem is a handful of application mills, consulting firms which saw an opportunity in a well-intentioned liberalization in FCC filing standards to produce cellular applications and mass market them on a nonexclusive basis as though they were tickets in a state-run lottery. In normal circumstance CTIA applauds entrepreneurial activity. Many of CTIA's members fairly can be characterized as entrepreneuers. But there are two facets of the application mills' "entrepreneurship" which are deeply objectionable. First, as Mr. MacLeod of the Federal Trade Commission testified on January 27, the advertising and related practices of certain of the application mills pose very real issues of legality. Second, the speculation which they induce has absolutely no redeeming value. As I mentioned on January 27, sometimes speculation produces socially useful results, as when speculators contribute to the liquidity of finacial markets. In cellular licensing, however, the speculation is merely a drag on the process, wasting the FCC's resources and creating delay which harms both consumers and producers of cellular service.

Against this background, I believe that additional valid requirements frankly designed in part to limit the application mills' "photocopy machine" approach to cellular applications is well warranted.

The application mills often have a three-pronged plan to maximize their profits at the expense of the licensing system and of their applicant-customers. First, they make money by selling the same application for the same market to hundreds of individuals. Second, they have contingency elements requiring a flat "success bonus" if the applicant wins. Third, they have additional contingency requirements that place them in the position of controlling the license's sale or legal work.

We think that preparers should not be allowed to have a contingency clause based on the success of the applicant in winning the lottery. This would protect the applicant, who basically has little or no knowledge of the process or of cellular service, and reduce the obvious conflict of interest on the preparers' part. It also would correspond with a pending FCC proposal to prohibit interests in more than one application in a market. The most direct way to do this is to prohibit and party from taking any interest in more than one RSA applicant, including one that is contingent on the successful award of a construction permit or license to that applicant.

Further, the applicant should supply a business address and telephone number along with disclosure of the identity of the applicant's principals. Too many times in the recent past, an application has contained only a signature; vital information about the applicant is missing. This additional information would be valuable in its own right, but it also would discourage the vending of undifferentiated applications on a cash-and-carry basis.

None of these recommendations would act to exclude anyone sincerely interested and qualified to build and operate a cellular telephone system.

Senator INOUYE. Mr. McAllister.

STATEMENT OF JOHN McALLISTER, PRESIDENT, WEST CAROLINA RURAL TELEPHONE COOPERATIVE

Mr. MCALLISTER. Thank you, Mr. Chairman. My name is John McAllister, and I have served since 1951 as President of the West Carolina Rural Telephone Cooperative, a locally-owned and -operated telephone company located in Abbeville, South Carolina. My company serves 6,000 customers in the counties of Abbeville, McCormick, and Anderson. I have also been a member of the Rural Telephone Bank Board since 1974.

I am here on behalf of my company and the United States Telephone Association, which represents approximately 1,100 local telephone companies, providing more than 99 percent of the local company-provided access in the United States. USTA members range in size from the regional Bell companies to the smallest of independents, and serve both rural and urban areas. Many offer or want to offer cellular telephone service.

82-856 0 - 88 - 4

I am also here on behalf of a group of 15 locally-owned rural telephone companies and cooperatives serving about a quarter of the area of South Carolina. I also speak on behalf of the Organization for the Protection and Advancement of Small Telephone Companies and the National Rural Telecom Association.

Metropolitan areas have benefited from cellular telephone service for several years, while rural areas have patiently waited for its availability. Having completed the licensing of the 305 metropolitan service areas (MSAs), the Federal Communications Commission is now ready to start the granting of cellular licenses for 423 rural areas (RSAs).

In the meantime, however, Congress has put a hold on that process, and this Committee is investigating the Commission's plans.

Mr. Chairman, America's rural telephone companies traditionally have held one objective: to serve customers throughout their service areas. For years, rural customers did without telephones, until small companies and cooperatives all across America emerged to fill that void.

Until now, small companies have had no opportunity to offer cellular service. They were unable to compete for MSA licenses, and now their ability to provide cellular on the same universal basis as they do wireline service is threatened by the big non-wireline companies in adjacent areas that are primarily, if not solely, interested in the heavily traveled corridors and more densely-populated areas of the RSAs.

This is the last chance for the small companies to be part of the cellular revolution. Unless they are given a fair chance to serve these more densely-populated areas and corridors, along with these sparsely-traveled areas, their ability to provide any cellular service at all will be seriously handicapped.

Several of the largest, established non-wireline companies have proposed that only non-wireline franchises in adjacent MSAs should be able to apply for RSA non-wireline licenses. Today we have heard additional variations on this theme.

One of the proposals suggest a two-tiered lottery. First, all non-wireline (non-telephone company) applicants would be subject to a lottery.

Second, the winner of that lottery would be required to enter a second lottery against the adjacent non-wireline MSA cellular licensee. This places the present non-wireline MSA licensee in a position to sit back and let the other non-wireline applicants for the RSA battle it out in the first lottery, and then enter a second lottery solely against the winner of the first lottery.

This assures the present non-wireline MSA licensee of, at worst, a 50–50 chance of winning the RSA license. Such a proposal is extremely biased in favor of the present and usually large MSA non-wireline licensees.

In general, these proposals would eliminate virtually all of the competition for these licenses and grant these companies a Congressionally-mandated preference. Clearly, this kind of proposal benefits only its proponents. It would hurt virtually all others interests involved in the technology, especially the public.

These proposals would damage consumers in two ways. First, Congressional action would mean additional delays while a new

rural cellular licensing policy is legislated and executed. Already the Congress has halted the process three months. Even if a law were quickly enacted, the Commission would need additional time to promulgate rules consistent with the wishes of Congress. This would take many months.

Second, these proposals would most damage the interests of rural Americans who live and work beyond the fringes of the RSA/MSA borders. FCC rules do not require non-wireline applicants to provide universal service. Non-wireline franchisees would find that it would only make sense to market their service along highways and in densely-populated areas adjacent to their existing MSA franchises. Consumers in high-cost sparsely-settled parts of the RSA could be ignored by an expanding MSA-based company.

Consider, for example, that public phones are readily available in metropolitan areas, but along rural roads landline service generally is unavailable. It is certainly desirable to bring cellular service to these sparsely-settled areas, as it would further universal service. These proposals by non-wireline companies would prohibit the use of telecommunications technology to fulfill this important national objective.

We urge the Congress to reject the proposal of the large, non-wire-line companies, because they would damage the interests of everyone except their proponents. Congress should not legislate an exclusive preference. Congressional action would hinder rather than assist in expediting the expansion of cellular telephone service to rural America.

The same rules that applied to metropolitan areas should be applied to the rural areas without further delay. Thank you, Mr. Chairman, and your Committee.

[The statement follows:]

STATEMENT OF JOHN MCALLISTER, PRESIDENT, WEST CAROLINA RURAL TELEPHONE COOPERATIVE

Thank you, Mr. Chairman. My name is John McAllister, and I have served since 1951 as president of the West Carolina Rural Telephone Cooperative, a locally-owned and -operated telephone company located in Abbeville, South Carolina. My company serves 6000 customers in the counties of Abbeville, McCormick and Anderson. I have also been a member of the Rural Telephone Bank Board since its inception in 1973. I am here on behalf of my company and the United States Telephone Association, which represents approximately 1100 local telephone companies providing more than 99 percent of the local company-provided access lines in the United States. USTA members range in size from the regional Bell companies to the smallest of independents, and serve both rural and urban areas. Many offer or want to offer cellular telephone service. I am also here on behalf of a group of 15 locally-owned rural telephone companies and cooperatives serving about a quarter of the area of South Carolina.

Metropolitan areas have benefited from cellular telephone service for several years, while rural areas have patiently waited for its availability. Having completed the licensing of the 305 Metropolitan Service Areas (MSAs), the Federal Communications Commission is now ready to start the granting of cellular licenses for the 423 rural areas (RSAs). In the meantime, however, Congress has put a hold on that process, and this Committee is investigating the Commission's plans.

Mr. Chairman, we oppose any congressional proposal that would prohibit an interested entity from applying for a cellular license. It is inappropriate for Congress to establish an eligibility requirement. An exclusion of applicants would give an unfair preference to a handful of established cellular interests, and would damage rural customers and local telephone company competitors. The public would be best and most expeditiously served by allowing the licensing process to go forward without

Congress changing the rules. A change in the FCC rules will effectively eliminate the opportunity for consumers in remote areas to receive cellular service.

The Commission has long considered how to allocate fairly and promptly rural cellular licenses. While the cities were beginning to receive service, rural areas were still waiting for a workable licensing procedure. The initial tentative approach, of self-defined cellular geographic service areas, was rejected as inefficient and unworkable. The Commission also rejected a corridor approach that would grant licenses in rural areas located between MSAs. The RSA approach was finally adopted in 1986 as a fair and effective way to license all rural service areas.

To ensure competition, the Commission licenses two companies to provide cellular telephone service in each service area: one is a "wireline" franchisee, that is, a local telephone company operating within the RSA; the other is a nonwireline franchisee, which may include radio common carriers or other interests. Applicants for these licenses covering areas that have competing applications enter separate FCC-administered lotteries.

Last year's House Energy and Commerce Committee report on the FCC authorization bill recommended changing the rural licensing procedure. The Senate, during its consideration of the continuing resolution, also questioned the process. Meanwhile, several large nonwireline companies lobbied Congress to limit nonwireline applications to companies that already hold licenses in adjacent MSAs. These companies, claimed that their plan would reduce speculative applications and FCC processing time and would speed service to the public. These companies, it should be noted, control most nonwireline MSA licenses. For example, one company, McCaw Communications, holds 94 licenses covering MSAs with a population of 37 million people, the *Wall Street Journal* reported last August.

Congress did not agree to the nonwireline proposal but did adopt an amendment preventing the FCC from accepting RSA applications until March 22, 1988, on the rationale that the delay would allow Congress to examine the Commission's licensing procedure. Unfortunately, the delay gives the established large nonwireline companies another chance to reargue their case for a legislated limit on nonwireline applicants. This is particularly unnecessary since the FCC is considering new standards to ensure that RSA applicants are ready, willing and able to provide service.

The proposal of the established nonwireline companies would eliminate virtually all competition for nonwireline licenses and grant them a congressionally mandated preference. Clearly, this proposal benefits only its proponents. It would hurt virtually all other interests involved in this technology, especially the public.

This proposal would damage consumers in two ways. First, congressional action would mean additional delay while a new rural cellular licensing policy is legislated and executed. Already the Congress has halted the process for three months. Even if a law were quickly enacted, the Commission would need additional time to promulgate rules consistent with the wishes of Congress. This would take many months.

Second, this proposal would most damage the interests of rural Americans who live and work beyond the fringe of RSA/MSA borders. The nonwireline companies would find that it would only make sense to market their service along highways and in areas adjacent to their existing MSA franchises. Consumers in high-cost, sparsely settled parts of the RSA could be ignored by an expanding, MSA-based company.

Three groups of applicants also would suffer under the unfairness of this proposal.

Wireline MSA franchisees, the local telephone companies providing cellular service in metropolitan areas, would be hurt. They would face unfair competition in their own service areas from their nonwireline MSA counterparts, whose service area had been expanded by an act of Congress.

Similarly, rural telephone companies hoping to offer cellular service would face equally unfair competition from a congressionally mandated, combined MSA/RSA licensee. Local telephone companies, historically confined to local service areas, would find their most profitable cellular customers siphoned away by nonwireline companies offering service to an unfairly expanded service area.

All other potential nonwireline RSA applicants would be denied a fair chance to compete for a license. These would include non-wireline companies that serve nonadjacent MSAs and all other applicants, including aggressive entrepreneurs anxious to get into the business.

Mr. Chairman, America's rural telephone companies traditionally have held one objective: to serve customers throughout their service areas. For years rural consumers did without telephones, until small companies and cooperatives all across America emerged to fill that void. Until now small companies have had no opportunity to offer cellular service. They were unable to compete for MSAs, and now their ability to provide cellular on the same universal basis as they do wireline service is

threatened by big nonwireline companies in adjacent areas that are primarily if not solely interested in the heavily traveled corridors and more densely populated areas of the RSAs. This is the last chance for small companies to be a part of the cellular revolution. Unless they are given a fair chance to serve these more densely populated areas and corridors, along with the sparsely traveled areas, their ability to provide any cellular service at all will be seriously handicapped.

We urge the Congress to reject the proposals of the large nonwireline companies, because they would damage the interests of everyone except their proponents. Congress should not legislate an exclusive preference. Congressional action would hinder, rather than assist, in expediting the expansion of cellular telephone service to rural America. The same rules that applied to metropolitan areas should be applied to rural areas without further delay.

Thank you.

Senator INOUYE. Thank you very much. Mr. Stroup.

STATEMENT OF THOMAS A. STROUP, VICE PRESIDENT, TELOCATOR NETWORK OF AMERICA

Mr. STROUP. Mr. Chairman, Members of the Committee, thank you for this opportunity to appear before you this morning.

My name is Thomas Stroup and I am the Vice President of Telocator Network of America, a national trade association representing the Mobile Telecommunications Industry for the last 40 years.

Telocator's more than 650 members include nearly 40 cellular telephone companies ranging from operators of multiple systems to licensees of only a single market, and more than 200 providers of conventional mobile telephone service.

Telocator's members have three major concerns regarding the FCC's proposed licensing process for RSAs. Unless eligibility rules are tightened to screen the tens of thousands of applicants with little or no intention of providing cellular service, the quality of rural cellular service will be reduced. The cost to consumers will be significantly increased, and the service to rural America will be needlessly delayed.

The abuses of the FCC's past process have been well documented this morning. Application processors sold identical applications and recruited people that were not interested in cellular service previously and that had little or no interest in building these systems.

Indeed, three-quarters of the markets have actually been sold. And we have been able to identify only six systems that have been built and are now operating.

The costs to those companies that have had to purchase the licenses or construction permits have been in the millions of dollars per market.

So while the speculators reaped a windfall, the cost of each buyout was an additional expense for the legitimate operators that had to be recouped from subscribers. In addition, service was delayed as speculators bid up the price.

Telocator has submitted a proposal for the upcoming RSAs that would alleviate this problem. It would curb the abuse and would assure high quality service to rural America.

Our proposal, and I would like to note that there was a mischaracterization in the last panel regarding who was supporting this proposal, McCaw is not the only company that is supporting the proposal, but it is all of the members of Telocator.

Our proposal is to limit eligibility to those companies that have demonstrated an ability to construct and operate mobile telephone

systems—specifically, the adjacent cellular operators. They would provide a logical extension of their existing system.

I have submitted two engineering statements with my testimony that documents the efficiency of this type of extension.

In addition, conventional mobile systems, mobile telephone systems in the RSA that are providing interconnected mobile telephone service would also be qualified applicants.

The rationale for this group of applicants was discussed by Steve Seltzer in his earlier testimony. These companies have shown a commitment to the industry. They are not attempting to turn a quick profit.

They would provide the highest quality service. They have experience with the technical and marketing aspects of the business and the community. In addition, they would provide the quickest service to the public.

They would not be starting from scratch, and they would not be tied up in the bidding for the construction permit or the license. I need to emphasize that this is not a giveaway. There would continue to be competition for the licenses.

Indeed, there would be more RCC applicants than cellular applicants under this proposal. It would not be a giveaway to the existing cellular licensees, and it is not something for the companies that are currently in the business only.

If the FCC's rules are not changed, hundreds of thousands of applications will be filed. Serious operators with a proven track record will be given virtually no chance to obtain the license without buying it from the speculators.

This will, of course, result in a windfall to speculators by extorting the extravagant prices from existing cellular carriers and RCCs that are already in the RSA. And, of course, the cost to the public will be in the hundreds of millions of dollars.

The FCC's attempt to halt this abuse in the past has failed, and we do not believe that it can be cured in the future.

Pre-screening of applications is simply unworkable, given the magnitude of the applications that are expected. The FCC does not have the staff to review each of these applications individually.

Financial restrictions are easily met. The application processors have already indicated that they will offer partnership programs to allow their applicants to meet the FCC's financial criteria, even if they are strengthened.

Construction requirements are similarly unworkable. All it has resulted in in the past has been legal maneuvering to fulfill the transfer requirements, or else the cheapest system will be built, regardless of its compatibility with the existing system or the quality of service it would provide to the public.

The FCC recognized the need for transfer prior to construction, with respect to some MSAs, in order to bring service to the public most quickly.

Telocator's proposal, I would like to note Mr. McAllister's concern, would apply only to non-wireline authorizations. Neither wireline eligibility nor wireline procedures would be affected.

However, I would like to note that the FCC justified in part its separate allocation of cellular frequencies to wirelines on the basis of experience gained in providing basic telephone service.

Telocator's proposal likewise defines eligibility in terms of proven experience, but in the mobile communications industry. Thank you.

[The statement follows:]

STATEMENT OF THOMAS A. STROUP, VICE PRESIDENT, TELOCATOR NETWORK OF AMERICA

Mr. Chairman, Members of the Subcommittee. Thank you for this opportunity to appear before you this morning.

My name is Thomas Stroup. I am the vice president of Telocator Network for America, the national trade association representing the mobile telecommunications industry for the last 40 years. Telocator's more than 650 members include nearly 40 cellular telephone companies ranging from operators of multiple systems to licensees serving only a single market, and more than 200 providers of conventional radio telephone service.

Since the FCC first allocated spectrum for cellular telephone service, Telocator has worked for the development of a competitive industry. When the Commission initially proposed that only the established telephone companies would be eligible for cellular frequencies, Telocator argued successfully that the spectrum should be available to those who could demonstrate that they were qualified to construct and operate a cellular system.

The creation of so-called "wireline" and "non-wireline" frequency allocations in each market has prevented cellular from becoming another telecommunications monopoly. Instead, consumers can choose between two competing cellular systems, each offering its own array of services and prices.

As you know, the Commission has used a lottery to award cellular authorizations in all but the 30 largest markets in order to avoid the delays inherent in the use of comparative hearings. Lotteries have been held to grant licenses in the approximately 300 metropolitan markets in the U.S. Now the Commission is preparing to process applications to provide cellular service in more than 400 so-called "rural service areas."

Telocator supports the continued use of lotteries to award cellular authorizations. A return to comparative hearings among cellular applicants would produce enormous delays without necessarily resulting in the selection of the "best" licensee. Comparative hearings would encourage "gold plated" cellular proposals and would force the Commission to make an inherently arbitrary choice from among alternative plans for constructing and operating cellular systems that may not be directly comparable.

However, we are gravely concerned that the quality of rural cellular service could be reduced—and the costs to consumers significantly increased—unless the rules governing non-wireline cellular eligibility are tightened to screen out the tens of thousands of speculators who will apply for non-wireline cellular authorizations with little or no intention of actually providing service to the public.

We speak from experience.

Almost 100,000 non-wireline applications were filed in the smaller metropolitan markets. Most of these applications were prepared by firms that mass-marketed them to people who were told that cellular was a unique "get rich quick" opportunity if they won a license and could sell it to an established cellular operator. In most of these markets, that is precisely what happened. The "mills" that prepared and sold the applications organized their customers into "settlement groups" that, in three-quarters of the smallest 180 metropolitan markets, sold their authorizations to operators of cellular systems in adjacent metropolitan areas for several million dollars *per market*. (Some speculator groups had their systems built—most often by the potential purchasers—before selling them, but only because the FCC's rules barred the sale of a system before it was constructed.)

While the application mills and a few of their customers reaped a windfall, the cost of each such buy-out was an additional expense for the legitimate operator that had to be recouped from his subscribers. Service to the public was delayed as the speculators bid up the price for these small-market authorizations.

A recent brochure from the Mobile Telephone Corporation to its customers is particularly revealing. "The bottom line focus," it says, "is MONEY." MTC's promise to reveal "an offer [to purchase] that will knock your socks off" and its prediction that "[t]he cellular monopoly/poker/chess game is just beginning" demonstrate beyond any doubt that MTC's interest is not in providing high quality service to the public.

Unless Congress acts, this unfortunate history is going to repeat itself. The speculators have already begun to market applications for these rural markets, stressing the quick profits to be made by selling cellular authorizations. I have included excerpts from some of their brochures with my written statement. Let me give you just a few examples.

The mailing from Vega Cellular Consultants opens with a quote from *Fortune* magazine characterizing cellular as "a business in which it will be possible and perhaps even easy to get rich quick" and goes on to quote Mr. Vega's expectation that cellular will "make more millions for those who have learned how to position themselves to gain these enormous profits." Vega's business is positioning people to reap windfalls, not the operation of cellular systems.

Romulus, another application mill, invites foreign investors to "own[ ] a piece of the American Telecommunications Network." In apparent violation of the Communications Act, this brochure seems to offer non-U.S. citizens a 25% interest in cellular applications in each of the rural service areas. (The Act bars the grant of any broadcast or common carrier license to any corporation in which aliens own more than a 20% interest.) Far from offering "ownership" of a cellular system, moreover, Romulus stresses the profits to be made by *selling* cellular construction permits and licenses.

Finally, Brown & Finn offers a volume discount to customers who purchase applications for more than 10 rural markets. Brown & Finn's literature clearly illustrates where they think the "value" of rural cellular licenses lies. The strategic location of rural markets, they explain, "may mean the possibility of eventual merger with or sale to an urban operator who may be interested in consolidating systems in the immediate area."

The FCC estimates that between 100,000 and 200,000 applications will be filed for just over 400 rural markets. In fact, a "test" of the filing mechanism designed to accommodate this load, the Commission received more than 3,000 applications for only two markets—suggesting that the Commission's initial estimates of the total number of rural applications may have been substantially understated.

Clearly, the rules governing eligibility for the cellular lottery must be changed.

Telocator believes that the Communications Act's goal of rapid, efficient service to the public will be met only if eligibility for rural non-wireline authorizations are limited to non-wireline cellular licensees and permittees in metropolitan statistical areas adjacent to the rural service area and licensees providing conventional mobile telephone service, interconnected with the public switched network, in the rural service area. These entities have demonstrated the ability to construct and manage a mobile telephone system; they should be eligible by virtue of their expertise.

Let me explain why we believe that experience should define eligibility for these rural markets.

Most rural cellular systems are logical extensions of either the cellular systems serving the adjacent metropolitan areas or the operations of radio common carriers already licensed in rural areas to provide conventional mobile telephone service. Cellular and mobile telephone operators are already familiar with the technical and marketing needs of the community. They are the experienced businessmen and businesswomen who can deliver service to the public simply by extending their existing systems—either geographically or by adding new technology—to cover rural areas. Moreover, they could begin offering service quickly and with less expense than having to build new systems from scratch.

As Steve Seltzer testified earlier, radio common carriers have the experience in engineering, marketing, and service that is directly applicable to the provision of cellular telecommunications. Radio common carriers are familar with the special problems of providing mobile communications services in rural areas. They have experience in designing mobile communications systems to take into account terrain, weather, and other factors that can affect the quality of radio-based communications—including cellular. In many cases, they already own or have access to the best antenna sites in a rural area—sites that are or will be used for rural cellular service.

Radio common carriers also understand the needs of mobile communications customers, and have a marketing and service infrastructure in place that can be readily adapted to the provision of cellular service, which, after all, is really just conventional mobile telephone service using advanced technology. In fact, many of the services identified with cellular—like voice storage and call forwarding—are already being offered by providers of conventional mobile service.

The so-called "independent investor" brings none of this expertise to the difficult task of bringing advanced mobile communications services to rural America. To the

contrary, the track record of "independent investors" in cellular suggests that they have neither the experience nor the interest in undertaking this role.

Like the radio common carrier, the adjacent non-wireline cellular licensee or permittee can easily build upon his existing operations to provide rural cellular service. Indeed, the Commission itself has acknowledged that it often makes more sense to provide service to a small market in conjunction with an adjoining larger one, even though the cellular licensing scheme inherently assumed that each market could support a separate cellular system. For instance, the joint operation of adjacent larger and smaller markets dramatically reduces costs while at the same time providing the benefits of an intergrated system serving a broad community of interest that may include more than one metropolitan area. By contrast, the construction of a stand-alone system in the smaller market would be more costly (with the additional cost passed on to consumers). The provision of regional service would also be impeded if the smaller system were not technically compatible with the larger one.

To illustrate this point, I have attached to my testimony a statement from Harrell Freeman, who designed the non-wireline cellular systems for New Orleans and Baton Rouge. Mr. Freeman found that it was more efficient to operate the Baton Rouge system—serving a market with a population of 500,000—by using the switching facilities of the New Orleans system rather than constructing a stand-alone system. The Baton Rouge cells are linked to the switch in New Orleans by microwave radio. According to Mr. Freeman, this arrangement reduced the costs of constructing the Baton Rouge system by approximately 80% and reduced operating expenses by more than 50%.

What was true for the smaller metropolitan markets is also true for the rural service areas, if not more so. Rural service areas are essentially arbitrary collections of adjoining counties without significant population or commercial cohesiveness. The areas were created by the FCC solely for the purpose of awarding cellular licenses. In fact, many rural service areas contain counties that are in fact included within adjacent metropolitan areas.

Attached to my written statement is an assessment of the major issues surrounding the technical design of rural cellular systems prepared by Comp Comm, Inc., a consulting and engineering firm that specializes in mobile communications. Comp Comm's report discloses that continuous service between a rural market and an adjacent metropolitan area is possible only if the rural cellular system shares the adjacent urban system's switching facilities. If the rural system uses its own switch, it must be from the same manufacturer as the urban system uses—or there cannot be any communication between them.

Comp Comm's analysis shows that rural cellular service—including adequate coverage both of population centers and transportation arteries—can be provided more efficiently and cheaply by utilizing the switching facilities of an adjacent cellular system than by the construction of switch dedicated solely to the rural market. According to Comp Comm, the provision of rural cellular service in conjunction with an adjoining large-market system would assure high-quality service both to rural residents and "roamers" passing through the area—at a savings of $800,000 compared to the costs of constructing a stand-alone rural system.

Of course, a carrier experienced in mobile communications would understand the need to construct a rural cellular system that was compatible with the one used in the adjacent urban market. By contrast, a speculator with no intent of remaining in the market would likely construct the cheapest possible system without regard to compatibility with the adjacent licensees.

The speculators' total lack of experience in mobile communications, combined with the financial and technical constraints I just described, strongly suggest that the award of a cellular license to one of the so-called "independent investors" would offer little in the way of innovative engineering or services. By contrast, the costs of permitting them to participate in the lottery are substantial.

If the FCC's eligibility rules are not changed, tens of thousands of these speculators will apply for cellular authorizations in rural service areas. In the face of these thousands of speculative applications for these markets, the people with experience in mobile communications stand no real chance of being authorized to provide cellular service in their own markets.

Rather, speculators who win the rural cellular lotteries will reap a windfall again by extorting extravagant prices from cellular operators who need that rural market to "fill out" regional systems or from mobile telephone licensees who can provide cellular service as a natural extension of their existing business. That means that qualified companies—with a proven track record in providing service to the public—will have almost no chance to serve rural cellular users unless they pay the hundreds of millions of dollars that the speculators will demand from them.

If each of the rural market authorizations is sold by a speculator for $1 million—and many of the small urban markets sold for several million each—almost a *half-billion* dollars will be added to the costs of constructing and operating these systems. At least part of these costs will be passed on to consumers, and non-wireline carriers will find themselves at a competitive disadvantage—since the wireline carriers in rural markets will not have to carry this burden.

There are those who suggest that the number of speculators could be reduced if only the FCC imposed tougher threshold requirements on applicants for rural cellular licenses. Again, experience strongly suggests the contrary. In an effort to prevent or reduce speculation in non-wireline cellular applications, the FCC has continuously refined its application process to prevent or reduce the number of these filings.

For example, the Commission altered its standard for an applicant's financial showing from a "reasonable assurance" of available funds to a "firm financial commitment" in order to deter the filing of "purely speculative applications by thinly or noncapitalized entities." It imposed a requirement that all applications be "letter perfect" upon filing. It established guidelines for settlements among competing applicants in a market. Notwithstanding these efforts, however, extraordinary numbers of applications were filed.

We can expect that the speculators will likewise be able to post the performance bonds or make the showing of available funds that has been suggested to winnow out speculators. While these additional requirements might reduce the number of applications somewhat—three or four speculators might have to join together, for instance, to pay the fee required for a performance bond—that would still allow hundreds of applications to be filed in each rural market. As a practical matter, the odds of a qualified applicant winning the lottery would remain infinitesimal.

The plain truth is that so long as an applicant can rely on application mills and others (such as cellular system equipment manufacturers) to prepare applications at lost cost, construct facilities and run systems, large numbers of applications will be filed. The risk-reward ratio is still great enough to be attractive because the cost of getting into the process is low in comparison with potential gain to a system seller. The imposition of a "grant fee" payable by a cellular licensee prior to the commencement of service to the public would not significantly change that ratio—and would impose upon cellular operators a cost not placed upon any other user of the spectrum.

For these reasons, Telocator has concluded that the only feasible means of preventing speculation and assuring rural America access to high-quality cellular service is to limit non-wireline applications for the rural service areas to cellular and conventional mobile licensees, as I described earlier.

Our proposal would not guarantee anyone a non-wireline authorization. Rather, we would ensure that the competition for non-wireline licenses was among only the most qualified applicants. We estimate that there will be perhaps a half-dozen such applicants, on average, in each rural service area. Many of these applicants—certainly most of the radio common carriers serving rural America—will be the small businesses that should be encouraged to apply their expertise to this burgeoning industry.

Let me emphasize that Telocator's proposal applies only to eligibility for the non-wireline authorizations in the rural service areas. We do not propose to change the current standards governing eligibility for the wireline cellular block in the rural markets, or the procedures for awarding authorizations on the wireline block. It is worth noting, however, that the FCC justified the separate allocation of cellular frequencies for telephone companies in part on the basis of the experience they had gained in providing basic telephone service.

Telocator's proposal likewise defines eligibility in terms of proven experience.

Thank you. I would be happy to answer any questions you may have.

Senator INOUYE. Thank you very much. Mr. Blum.

STATEMENT OF THOMAS C. BLUM, GENERAL MANAGER, EXTERNAL AFFAIRS, BELL ATLANTIC MOBILE SYSTEMS, INC.

Mr. BLUM. Mr. Chairman, Members of the Committee, I appreciate the opportunity to present this statement on behalf of Bell Atlantic Mobile Systems, which is also known as BAMS. BAMS is a subsidiary of Bell Atlantic Corporation.

BAMS provides cellular service in a number of markets throughout the mid-Atlantic region. Near the geographic areas where BAMS provides cellular service, there are many rural service areas. For example, the eastern and western shores of Maryland are rural service areas, half of the State of Delaware, about half of Virginia, three quarters of Pennsylvania, almost all of West Virginia, and three counties in New Jersey.

BAMS' interest in testifying before this Committee is to ensure that cellular service to rural areas is made available as soon as possible.

We have heard a number of proposals today to limit the applicants eligible to apply to the FCC for non-wireline cellular authorizations. Restrictions on applicants, it is argued, would make the FCC's lottery selection system work better.

The FCC plans to use its existing lottery system to award cellular licenses for RSAs, and has announced a plan to start accepting applications for RSAs in February. This date was postponed once, and may be postponed again, given uncertainty surrounding what Congress will do.

If Congress reaches a decision quickly and does not change the already-in-place-and-tried FCC lottery system, then most of the RSA licenses can be awarded this year, and many rural service areas will have service this year.

But, if Congress does not reach a decision quickly, or changes the present method of awarding licenses, then cellular service to rural America may again be delayed, for who knows how long.

In support of adopting legislation, it has been suggested that creating new or different restrictions on non-wireline lottery applicants will reduce the number of applicants, thereby eliminating speculation. What has been suggested will not eliminate speculation, but will instead merely limit speculation to big companies already in business, without any benefit to the public.

It has also been suggested that limiting the number of applicants will speed up service to rural America. The FCC has established a lottery system to get service to the public as soon as possible. In fact, the FCC is ready to issue licenses now. To change that system would involve more rather than less delay. Any change would involve new rules and the delay and disruption inevitable in formulating and implementing them, as well as delay created by what will almost certainly be numerous judicial challenges.

It has been suggested that legislation would ensure that only experienced cellular providers could provide RSA service. The cellular industry is in its infancy, and therefore most of these cellular experts have less than two years of experience.

It has also been suggested that stronger requirements with respect to an applicant's financial showing or raising the application fee may help weed out speculative or "insincere" applicants. This may be true. But it is difficult, if not impossible, to know where to set the standard in order to sort out effectively and appropriately such applicants. And I think we could argue about this forever.

Any changes to the present system, whether by legislation or otherwise, will not only cause delay, but will also cost consumers money. In fact, such changes will almost certainly result in litigation.

To relitigate a new methodology used by the FCC to issue cellular licenses could take as long as two years with the court review. To relitigate this issue will cost both business and government many dollars, and consumers will get the final bill.

The public wants cellular service now. Delaying service to rural America will not benefit the public. For these reasons, BAMS urges that the limited resources of the FCC not be further burdened by attempts to fashion a new method of awarding cellular licenses at this twelfth hour. And I really believe this is the twelfth hour.

The FCC should be encouraged to proceed promptly, with existing procedures, to award cellular licenses for rural service areas. Thank you.

[The statements and question and answer follow:]

STATEMENT OF THOMAS C. BLUM, GENERAL MANAGER/EXTERNAL AFFAIRS, BELL ATLANTIC MOBILE SYSTEMS, INC.

Mr. Chairman, and Members of the Committee, I appreciate the opportunity to present this Statement on behalf of Bell Atlantic Mobile Systems, Inc., which is usually known as BAMS. BAMS is a separated subsidiary of the Bell Atlantic Corporation.

BAMS subsidiaries, or partnerships in which a subsidiary is a participant, hold wireline cellular mobile telephone authorizations and provide cellular service in a number of Metropolitan Service Areas (MSAs) in the Mid-Atlantic region, including, for example, Washington, D.C., Baltimore, Philadelphia, Pittsburgh, Trenton and Wilmington. The Washington, D.C. metropolitan area, as you know, was one of two areas where experimental licenses were awarded, and where there has been cellular service for more than a few years. BAMS also has interests in wireline licensees in other areas, such as New York and Virginia.

Near the geographic areas where BAMS affiliates provide cellular services, there are many Rural Service Areas (RSAs). For example, in New Jersey, there are 3 RSAs; in West Virginia, 7 RSAs; and in each of Pennsylvania and Virginia, 12 RSAs. These areas do not now have cellular service. BAMS' interest in testifying before this Committee is to ensure that cellular service to rural areas is made available as soon as possible.

BACKGROUND

Various members of Congress and others have indicated an interest in limiting the applicants eligible to apply to the Federal Communications Commission (FCC) for non-wireline authorizations to construct cellular mobile radio systems in Rural Service Areas (RSAs). Restrictions on applicants, it is often argued, will make the FCC's lottery selection system work better.

Presently, when more than one entity applies for a cellular license in a given area, the FCC holds a lottery to determine who will get the license. After years of rulemakings, litigation, changes in its statute, and trial and error, the FCC adopted its lottery system as the most expeditious, fairest, and least expensive method to get cellular service to the public. The FCC plans to use this system to a ward cellular licenses for 420 RSAs and has announced its plan to start accepting applications for RSAs in February. This was originally planned for December, 1987; then postponed to January, 1988; and then postponed to February, 1988. Given the uncertainty surrounding whether Congress will act, and if so how, the FCC once again may have to postpone this date.

If Congress reaches a decision quickly and does not change the already in place and tired FCC lottery system, then most of the RSA licenses can be awarded this year, and many rural areas can have cellular service by the end of 1988.

If Congress does not reach a decision quickly or changes the present method of awarding licenses, then cellular service to rural America may be again delayed, most likely into 1989 and 1990.

PROPOSED LEGISLATIVE CHANGES

There has been much discussion of changing the FCC RSA lottery system by, for example, restricting eligible applicants to only those entities already licensed to operate a cellular system, or only those entities licensed to operate a cellular system

in an area adjacent to an RSA, or by increasing dramatically the fee for filing a cellular application, or by raising the standards for determining if an applicant is technically, legally or financially qualified to be a cellular licensee.

SOME ARGUMENTS FOR AND AGAINST SOME PROPOSALS FOR LEGISLATIVE CHANGES

In support of adopting legislation, it has been suggested that creating new or different restrictions on non-wireline/lottery applicants will limit speculation in cellular authorizations and thereby reduce the number of applicants. Previously, there have been hundreds of applications filed in a single cellular market, as well as frequent sales by cellular lottery winners of cellular construction permits prior to, as well as after, construction of a cellular system. These, and other, actions have given rise to the view that the FCC cellular lottery process has led to speculation, and not to prompt provision of service to the public. In fact, large companies, such as Metromedia, and other smaller companies, have had interests in cellular licensees, which they later sold. But what has been suggested will not eliminate speculation, but will instead merely limit it to sales (and purchases) of cellular authorizations by large, rather than small, companies.

It has also been suggested that limiting the number of RSA applicants will speed up service to rural America. The FCC has established a lottery system to get service to the public as soon as possible. To change that system now would involve more rather than less delay. Any change would involve new rules, and the delay and disruption inevitable in formulating and implementing them, as well as delay created by what will almost certainly be numerous judicial challenges. Creating new rules to reduce the number of RSA applicants and eliminate "insincere" applicants in all 420 RSAs may not be as necessary as some have believed: the economic potential of all of the RSA markets, because of their small size, and other factors, may not be attractive to many investors, and, therefore, there may not be a vast deluge of applications for all of the RSAs.

It has been suggested that legislation would ensure that only "experienced" cellular providers could get RSA licenses. Does Congress want to establish a policy of letting only "experienced" companies provide cellular service in rural areas? The cellular industry is in its infancy; therefore, most cellular "experts" have less than two years experience.

It has also been suggested that stronger requirements with respect to an applicant's financial showing or the application filing fee may help weed out speculative or "insincere" applicants. This may be true. But is difficult, if not impossible, to know where to set the standard, in order to sort out (effectively and appropriately) such applicants. More importantly, however, as discussed, any change in FCC rules is likely to result in more delay in getting service to the public, as well as greater costs. Therefore, there type of changes are not likely to yield the hoped-for benefits to the public.

Changes to the present system, whether by legislation, or otherwise, will not only cause delay, but also will cost consumers money. In fact, such changes will almost certainly result in litigation. To relitigate a new methodology used by the FCC to issue cellular licenses could take as long as two years, with court review. To relitigate this issue will cost both business and government many dollars. Consumers will get the final bill. Where is the public interest in this?

The public wants cellular service now. Delaying service to rural America will not benefit the public's interest.

For these reasons, BAMS urges that the limited resources of the FCC not be further burdened by attempts to fashion a new method of awarding cellular licenses at this twelfth hour. The FCC should be encouraged to proceed promptly with existing procedures to award cellular licenses for Rural Service Areas.

SUPPLEMENTAL STATEMENT OF THOMAS C. BLUM

This supplement is submitted to correct certain information provided in statements and testimony furnished to the Subcommittee in connection with its hearing on Federal Communications Commission (FCC) licensing procedures for Rural Service Areas (RSAs).

These statements and testimony create the misconception that the dispute over how best and most rapidly to provide cellular service to rural America involves a battle between carriers such as McCaw Cellular Communications, In. (McCaw) and the Bell Operating Companies. (See, for example, the Statement of John E. McCaw, Jr. at page 13). The assumption is made that BOCs have assurances that they will

receive RSA licenses needed to fill in gaps in their coverage areas, including areas in which there are, for example, interstate highways.

In fact, many of the 420-odd RSAs cover areas served only by independent telephone companies. BOCs can not apply for RSA licenses in those areas. Indeed, there are approximately 1,500 independent telephone companies. These companies provide service in much of rural America, and are not dependent on the BOCs.

Accordingly, it is these independent telephone companies, not the BOCs, that McCaw, the largest non-wireline carrier in the country, (and other cellular carriers) will be competing against in a large number of RSAs. The testimony of John McAllister, President of the West Carolina Rural Telephone Cooperative, representing that organization and the United States Telephone Association, makes this point clear. The role of independent telephone companies in RSAs is also shown by the Statement of Steven G. Bowers, Chief Engineer and Vice President, Moultrie Independent Telephone Company.

As set forth in my prior statement, changes made now to the FCC RSA licensing procedures will only delay service to the public. The public wants cellular service now. Delaying service to rural America will not benefit the public.

QUESTION OF SENATOR PRESSLER AND THE ANSWER

Question. Do you have any alternative proposals for limiting speculation without eliminating serious competitors or putting an undue burden upon their involvement?

Answer. The FCC has suggested many plans to limit speculation and still get service to the public quickly. The Commission has proposed limitations on the formation of post filing settlement groups and the transferability of cellular radio applications as well as restrictions on the interests one entity may have in the RSA applications of another entity. Also being considered is raising the application fee (now $200) and imposition of a grant fee. Additionally, the FCC has released a rulemaking notice on February 19, 1988, redefining the appropriate financial qualification standards applicable to RSA applicants.

The above FCC suggestions and recently released Order will help curtail speculation without eliminating serious competitors or putting an undue burden upon their involvement.

It is not possible, particularly in a lottery system, to eliminate every possible abuse. The FCC has made some useful suggestions that should improve the present lottery system.

It is important that we do not make unnecessary changes in FCC rules that are likely to result in more delay in getting service to the public, and greater costs. Rural America has waited long enough for cellular service.

Senator INOUYE. Thank you very much. The FCC has testified this morning that a procedure is in place to determine the sincerity or the qualification of applicants or successful lottery winners.

The FTC has testified that investigations have been underway and ongoing to charge those civilly or criminally with scam operations or fraudulent operations. Assuming that the testimony is correct, what is wrong with speculators under our free enterprise system?

Mr. MAHER. I would like to address that, because speculators and entrepreneurs and the little guy have been intermingled here.

Speculation in a market, in the financial market, brings depth to the market. It is a good thing. But speculators and entrepreneurs and "the little guy" in this instance are separate things.

The entrepreneur can be a little guy who has great confidence in something, and he will go in. But he does one thing a speculator does not do in the case of cellular. He puts his finances behind it.

An entrepreneur will go out and buy part of a company or idea, or he will finance something. And that is part of what makes small business work. That is what makes small businesses turn into Apple Computers.

I do not think that somebody that puts up $400 can be called an entrepreneur. In other words, there is a basic difference here. Speculation on something where you have to back it up, with investments going in, is normal and desirable.

But simply to put up a couple of hundred dollars and use the system as a lottery I do not think is good. By doing this, the speculator is mathematically eliminating entrepreneurs and others who are qualified. And when I say that, I do not mean just the people that hold license now. I include qualified entrepreneurs.

There are many qualified people that might want to get into cellular. As long as they are willing to prove they are qualified, that they have available to them the money to build and operate a system, they have the personnel to do it, then they should not be omitted.

But if they do not, if it is an individual who puts up $400 with an application mill and calls himself an entrepreneur, I do not agree with that. Because that man is not qualified or capable of building and operating a cellular system. He is a speculator.

Senator INOUYE. However, is it not also logical to suggest that if I am a successful applicant, and I win the lottery, and although I may be limited in my finances, once I am a successful applicant, I will have droves of people who will want to invest in me?

Mr. MAHER. That is right.

Senator INOUYE. So finances would not be a problem, would they?

Mr. MAHER. It goes back to the problem, are you qualified before the lottery. Originally the requirements were that you be qualified to get into the lottery. That is a very big point.

Senator INOUYE. What is your idea of qualification?

Mr. MAHER. Someone who can demonstrate that they have the financial ability to construct and run a system for a year. And that entails the operating personnel.

When these applications were originally filed, they literally were two and three feet tall, and they cost $100,000 and $200,000 to put together because they were comparative hearings.

Senator INOUYE. In other words, you would have to be a millionaire before you file an application?

Mr. MAHER. No, not at all. But you would have to have access to financing.

Senator INOUYE. Well, would it not be logical to say that if I win I would have more than enough access?

Mr. MAHER. By winning you could be qualified. But if that were the case, if we are worried about financial barriers then why not do it on Social Security numbers, and let everybody in?

Mr. STROUP. Mr. Chairman, I would like to add to that. I think that there is a disadvantage to allowing the speculators to submit these applications, and that is a cost to the public.

It is the subscriber that ends up paying the cost, that the service provider has to pay to obtain the construction permit or license. And in addition, it results in a delay. The process results in a delay of cellular service to the public.

Now, I think you presupposed that the FCC's process does work. I think the facts indicate otherwise. We would not be here discussing the problem if the FCC's process did work.

Senator INOUYE. What is the average cost to a subscriber?

Mr. MAHER. For a speculator?

Senator INOUYE. No. To have a cellular telephone, what will it cost me?

Mr. MAHER. About $140. Well, about $140 is a national average. I cannot speak about your personal use, but on average about $130 or $140 a month.

Senator INOUYE. How much for the instrument?

Mr. MAHER. They go as low as $425 for a standard set to a portable that will run over $2,000, but it can be purchased for $1,700 or $1,800 at the low range.

Senator INOUYE. Of that $140 a month, what amount is due to speculation?

Mr. STROUP. Senator, we have not made that calculation. However, we would enjoy the opportunity to submit that evidence.

Senator INOUYE. Well, you said a substantial portion of that is due to speculation. I just want to know how much.

Mr. MAHER. Someone did do a study, Daniels Associates in Denver, a year ago, as a matter of fact.

They set up a model based on the assumption that whoever bought the license paid $20 per pop. And they put how much the price was, how much to service the debt, etc. and it came up to $350 per subscriber per year. And what that does is push the break even time of a system back about four to six years, in this hypothetical.

But someone has figured out what happens to a system that has to purchase as its first capital investment a license based on $20 a pop.

Senator INOUYE. Having heard from all sides of the issue, would you say that it would be possible to come up with a solution that would meet with the approval of all interested parties? Or are we called upon to make a decision one way or the other?

Mr. MAHER. No one has testified that speculators should have the right to apply if not qualified, and no one certainly admits to being a speculator. There is agreement here.

Senator INOUYE. I think the Committee has indicated that they would be against speculators. But they would like to have all Americans who want to make a few bucks have an opportunity.

Mr. MAHER. Some of those application mills have gone over to Geneva and told non-Americans that they can own 25 percent of a cellular telephone license and they can file in all the markets for $125,000.

My point is, if we should have criteria that people feel are fair and reasonable. The biggest hurdle is reaching an agreement on how to get criteria to insure you qualified before you are allowed into the lottery.

We feel very strongly you should. Because that piece of paper, the license, basically would qualify a monkey. You can go to any bank with an MSA license and get financing. No disrespect, if you were a barber, tree trimmer or truck driver, with an MSA license, that is almost bankable.

In the RSAs it will be harder. And a lot of the application mills are not explaining this to the people that they are selling to. They quote the prices paid for some of the nicer MSA markets. Unfortu-

nately some of them even demand that you buy applications for all 423.

So a lot of people think they are going to get parts of lucrative markets, when indeed some of their markets probably may not survive. But I think that if you get qualifications that everybody feels comfortable with, that are reasonable, non-exclusionary, that includes financing for personnel and so on, I think people can agree to that.

Senator INOUYE. Do you not believe that the right to file a petition to deny would weed out the unqualified?

Mr. MAHER. No, sir.

Mr. STROUP. Senator, Mr. McCaw mentioned a position that I think would possibly be workable, something that has been discussed amongst representatives of the industry and we will continue to discuss it with all parties interested in this proceeding.

And that is the dual lottery approach, which would allow the FCC to accept the applications of those people that have not established anything other than minimum qualifications. And then they would be entered into a grouping with those people that have established their qualifications via their prior service in the mobile services industry. We think that that perhaps has some merit.

Senator INOUYE. Mr. Blum?

Mr. BLUM. Yes, Senator. I would like to respond to your previous question. Is it possible that there would be a consensus, that everyone would agree to something?

I think it has become obvious to me even before this meeting, but even after this meeting more so, that the testimonies offered, that there are many points of view here, and there is no way they will all be reconciled.

And if any changes are made, we will have all types of litigation and all types of special interest groups coming in, and this will only delay the service to the public. I really think we can get service to most of the public in a lot of the rural service areas by this year, if we do not do anything.

If we make changes, I do not think we will get a consensus point of view that everyone will agree to.

Senator INOUYE. So you are suggesting status quo?

Mr. BLUM. Yes, sir. We are in the business to provide service and want to provide service. If these changes had been made, as suggested three or four years ago, I probably would not be here today.

But that at this twelfth hour, I think what they will do is delay service to the public, and that is not what we want. We do not want to delay service to the public.

Senator INOUYE. Mr. McAllister, do you want to add to that?

Mr. MCALLISTER. Certainly we do not want to delay service to the public, and I want to speak in regard to the rural areas of the whole country. These corridors are trying to get them.

But my real concern is the smaller areas that nobody wants to serve except the wireline people, that are adjacent. Say in South Carolina, we have four different MSA wirelines, and the corridors of South Carolina would be served. But the rural areas of this country would be left out.

Mr. MAHER. What he says is absolutely correct. A study done late last year, gives best case estimates and worst case estimates.

The study shows that thirty-seven percent of the RSAs probably will have less than 1,000 subscribers after five years. It is very hard to put up a system that is going to cost you at least $1 million in all probability, and look for a break even point well beyond five, six, seven years. And like I say, he is correct.

Mr. STROUP. Everybody's goal is to provide service to the public as quickly as possible.

It is a question of whether the problem is addressed now or at some future date, when we have to deal with the purchases from the speculators, the low-quality systems built to comply with minimum FCC standards.

We would like to see the problem addressed now so that the public will receive service quickly, and the highest quality service.

Senator INOUYE. The record will be kept open until the 15th of February, so that if any of you who have testified would like to submit additional information or statements or supplementary statements, feel free to do so.

Mr. MCALLISTER. We certainly will, sir.

Senator INOUYE. I have been advised by Members of the Committee that they would like to submit questions for some of you to respond to, so if they do I hope you will do so.

I would like to thank all of you for participating in this hearing. We will do our best to try to resolve this matter. But it would be helpful to us if the interested parties could get together and suggest a consensus agreement. It might be easier that way. Thank you very much.

[Whereupon, at 12:05 p.m., the hearing was adjourned.]

ADDITIONAL ARTICLES, LETTERS, AND STATEMENTS

STATEMENT OF STEVEN G. BOWERS, CHIEF ENGINEER AND VICE PRESIDENT, MOULTRIE INDEPENDENT TELEPHONE COMPANY

I am Steven G. Bowers, Chief Engineer and Vice President of the Moultrie Independent Telephone Company (Moultrie). I am pleased to submit this written statement to the Senate Committee on Commerce Science and Transportation, concerning proposals which Congress may wish to consider in order to prevent the filing of speculative applications for licenses to provide non-wireline cellular service in the rural service areas (RSAs) of the nation. Although Moultrie shares concerns regarding the filing of such speculative applications, we suggest that Congress carefully tailor its solutions in order to avoid inadvertent harm to our company, our subscribers, and other potential cellular service users throughout rural America.

Moultrie is a local telephone company serving subscribers in and around Lovington, Illinois. Moultrie is in an RSA which is virtually surrounded by four Metropolitan Statistical Areas (MSAs). As is the case with many of our rural telephone company colleagues, we have an interest in being able to utilize cellular technology to bring improved and expanded communications services to our rural subscribers. To the extent, therefore, that Congress makes policy recommendations or fashions solutions addressing the filing of speculative RSA applications, such recommendations or solutions should not harm our company, other similarly situated rural independent telephone companies, and future rural cellular customers.

Ultimately, the competition for providing cellular service to the public within any RSA will be between the non-wireline licensee and the wireline licensee. Non-wireline applicants and licensees are likely to argue that it is inequitable to impose restrictions and rules on the non-wireline application and license process that are not made applicable to their wireline counterparts. However, such a position does not address the fact that speculative applications have been effectively limited to the non-wireline cellular process.

Further, we are concerned that placement of restrictions on the wireline side could result in foreclosing many independent telephone companies from participating in the provision of cellular servive as a result of either revised eligibility restrictions or financial hardships these proposals could encompass, or a combination of both. To the extent that Congress seeks solutions which would include high application and/or license fees for the provision of RSA cellular service, this could result in direct and inequitable harm to rural Americans. The future rural cellular providers who pay these fees will inevitably recover these costs through increased rates they charge their subscribers. Moultrie believes that it is patently unfair for rural Americans to have to bear such costs when no similar fees were charged with respect to the privilege of providing cellular service in the more economically lucrative MSAs throughout the country. The addition of these costs may, in fact, discourage the implementation of cellular service in much of rural America where there is presently only marginal economic feasibility for its provision.

We believe that there are rational alternatives available to these proposals which more directly address the problem of speculative applications, and which would not pose the potential for harm to small rural independent telephone companies and their subscribers. For example, the FCC can adopt strict "non-trafficking" rules for RSA licensees. Moultrie envisions rules similar to those adopted for broadcast licenses. These rules have generally been successful in preventing speculative applications. Adoption of similar strict rules and policies for the non-wireline RSA process could be easily established. We thus believe that potential speculators could be deterred from filing non-wireline applications by preventing licensees from selling the license for profit until the cellular system has been operating for a prescribed period of time. This period of time could be set for as long as necessary to effectively eliminate speculation.

In conclusion, Moultrie believes that legitimate concerns about speculative non-wireline RSA applications should be addressed, as proposed above. Moultrie submits, however, that this Committee should assure that any resolution of this problem does

not result in any unwarranted and unnecessary harm to small, rural independent telephone companies and their rural subscribers. Finally, Moultrie respectfully urges Congress to make it clear that any action it undertakes to resolve the problem of speculative RSA cellular applications is expressly limited to the non-wireline process.

STATEMENT OF LEO BUK LHU, EDITOR OF CELINTEL NEWSLETTER AND MANAGER OF THE CELLULAR COMPUTING DATABASE

Why would anybody want to change the current procedure for awarding Cellular Telephone Licenses, now that the faults have been remedied? I spent a week in Pittsburgh observing the latest filings where I noted 1,861 applications for #257 and 1,849 for #269, with a $200 filing fee each, it appears the FCC discovered a popular tax! If alliances are continued, the Treasury will take in over $100 million, but without alliances for the 430 RSA licenses, there will only be about $40 million in filing fees.

Why give preference to prior Cellular License winners, when the previous lotteries were infested with cheaters? It may take years for the FCC and the Department of Justice to finish the investigations I started, but there was no evidence of lottery stacking at the January 11-15th filings. An unprecedented number of applicants actually bought engineering from the following: Eldon Heinz's engineering was used 490 times each, Gene Greenwell 226, Tom Adcock 218 for #257 and 217 for #269, Terry Easton 178, Rusty Irwin 158 for #257 and 154 for #269, and Darrell Bauguess sold about 150 pairs. Even without counting other engineering firms, these six provided bonafide work for ¾ of the applicants, a radical departure from prior lotteries where up to ¾ of the applications were given away for certain licenses (this includes the MSAs where there were over a hundred unauthorized copies made of that application) thereby stacking the deck against paying applicants.

It has taken a lot of time and money for applicants to finally get a fair chance to obtain a license and I feel that the more open the process is, the more likely new blood will dilute the crooks of the past.

STATEMENT OF THE MINNESOTA TELEPHONE ASOCIATION

The Minnesota Telephone Association is the trade group of the 94 local exchange telephone companies in the state. The MTA was formed 79 years ago to aid in the development of universal and high quality telephone service throughout all parts of the state, including rural and urban.

In 1986 the Board of Directors formed a cellular committee to address issues associated with this new communications technology. Issues at the Federal Communications Commission and Congress surrounding the rural cellular licensing process have come to the committee's attention. These issues concern the Minnesota Telephone Association. We ask that the views expressed in this position statement be considered in the amendment of FCC Rules or enactment of legislation by Congress.

Eighty-four of our member companies are actively involved in developing rural cellular systems in Minnesota. These companies have a proven commitment to providing high-quality state-of-the-art telecommunications services to rural communities and customers. They have a long-term interest in providing cellular service to their existing customers as well as any new telecommunications services that will appear in the future. Our member companies are uniquely suited to offer and jointly provide the rural areas of our state with a contiguous operating cellular network which provides low cost reliable service to all rural subscribers.

We oppose any legislation that provides an unfair advantage for large companies over small companies because this would discourage competition and may prevent many rural citizens from receiving cellular service. We realize that some of the proposals being considered presently are not directed toward wire-line providers. However, we are concerned that such proposals, if enacted, would ultimately apply to wire-line as well as non-wireline providers.

Historically the FCC has endeavored to make fair and equitable decisions when promulgating regulations for competing parties as they attempt to provide various telecommunication services to consumers. Therefore, it is reasonable to expect that restrictions applied to non-wireline providers will also be applied to wireline providers.

We support the current FCC rules on rural cellular services and request that they not be amended.

The following are critical concerns to us:

(1) We oppose large licensing fees or unreasonably high bank lines of credit because: Such fees discriminate against rural areas. Cellular providers in metropolitan areas were not subjected to these fees, and it is not fair to ask rural providers and subscribers to bear these extra costs; and increased license costs will only limit the number of rural citizens who ultimately receive this service.

(2) We oppose changing current eligibility requirements for the RSAs because: Current proposals would prohibit rural minority license holders in the MSAs from serving adjacent RSAs; and limiting non-wireline eligibility in RSAs adjacent to the non-wireline cellular provider would give the non-wireline provider a head start and unfairly limit competition in the less viable RSAs.

(3) We support the application of the rules as they were in the MSAs. We encourage fair and equitable procedures in issuing RSA licenses.

STATEMENT OF GEORGE M. BATSCHE, PRESIDENT, COMMUNICATIONS TRANSMISSION, INC.

As President of Communications Transmission, Incorporated (CTI) I would like to take this opportunity to express my gratitude to this Committee for permitting me to explain why I believe that there is now a tremendous opportunity for the Federal Communications Commission to create a nationwide system of cellular service along the federal interstate highway system. However, I believe that the method that the FCC has established for awarding construction permits for cellular systems by lottery will frustrate this goal.

CTI is one of the larger interexchange common carriers (IXC's) in the United States. As the attached map reflects the CTI network presently has over 4,500 miles of route served by the microwave stations. With the institution of competitive IXC service it was only logical that carriers would first try to obtain customers in the metropolitan areas. Since these cities are interconnected by the federal interstate highway system, it was equally logical for convenience of maintenance and ready access to electrical power that the carrier would try to place the microwave radio station as close to the federal interstate highway as practical. Any driver along the interstate system can generally see a microwave tower belonging to some IXC carrier to be found about every twenty miles.

A cellular system which has a single cell in a city can still function because it can connect the truck or car into the telephone network. A cellular system in a rural area with a single cell is useless unless that cell can be connected to the telephone network. Without this network connection a telephone call can neither be sent nor received.

The microwave station is, to the best of my knowledge, the only practical way to permit cellular phones on cars or trucks moving along the federal interstate highways to have access to the telephone network. A typical microwave station has eight microwave radios which provide a chain of transmission of both analog and digital information. It is industry practice not to lease a small portion of each radio, but to reserve it for other uses such as the transmission of alarm data—such as unlawful entry, power failure, etc. On an analog microwave system generally 300 of the 2,700 channels of voice/data capacity are reserved for this purpose. However, where a carrier has the full complement of eight 6 MHZ microwave radios generally used for long distance service, 1,800 reserve channels lie idle and only 600 are used for alarm purposes. The existence of these microwave radios along the federal highway is an essential element of the provision of interstate highway cellular service.

A car or truck going at 60 miles an hour along an interstate highway will come into and go out of the range of a single cellular radio every 30 minutes (15 miles before and 15 miles beyond the cell). Because 15 miles is the normal efficient range of a cellular radio the coincidence that high quality microwave transmission requires that the microwave towers be spaced between twenty and twenty-five miles means that microwave stations are ideal locations for interstate highway cellular systems.

A microwave station is an existing entity consisting of a purchased or leased site on which a tall tower has been constructed. The site is fenced and an auxiliary generator with battery backup installed. CTI maintains a full-time maintenance crew and spare parts depot in the community located nearest to the mid-point of every seven microwave stations, thus providing a high standard of maintenance.

Because a vehicle moving at 60 M.P.H. would rapidly go from cell to cell, a switching network capable of true cellular switching, is the *sine qua non* of providing cellular service on the federal interstate system. The now almost typical FCC cellular lottery application, specifying but a single cell to qualify for a chance at the

lottery, could not provide such service. An entire chain of such cells along the highway is absolutely necessary. Because of the reserved microwave channel capacity the cellular radio on the tower can be readily interconnected to a central cellular switch and, also, the cellular telephone message can be picked up from the cellular radio, modulated onto the microwave radio, and, thereby, relayed into the nationwide telephone network at the nearest telephone switching center. Thus, the microwave radio not only permits switching from cell to cell, which is essential for highway cellular service, but also the ability to carry that message from the cellular radio to the telephone network or to other vehicle along the system.

In order to realistically provide cellular service along the interstate highway system in the rural areas of the United States, the microwave plant built by the various IXC carriers, such as CTI, is an indispensable element. There simply is no other means of getting the communication from the cellular radio back to the telephone toll network, and vice-versa. However, under the FCC's lottery rules, such a proposal is impractical.

Since there are only eight duplex MHZ channels available, and these have an interference range of approximately 75 miles, only one IXC carrier is normally found along any single federal highway. This carrier does not provide exchange service and, as such, is only eligible under the FCC's rules for the non-wireline carrier cellular frequencies. For this interstate highway cellular system to be practical, the IXC microwave carrier must obtain not just a single FCC construction permit, but one located along the federal interstate highway in every RSA through which the microwave system passes. With the multitude of existing microwave stations along the federal interstates it would be soon possible for such carriers, by interconnecting carrier agreements, to allow a cellular telephone, on a single vehicle, to be used every day, at every hour that vehicle is moving from coast to coast. However, such a system is impossible under the FCC's present lottery system which does not consider which is the best applicant, but prefers the simple choice of the luckiest applicant.

Since IXC stations are located in very isolated areas along the federal interstate system, it appears to me that the IXC provider of cellular service is not truly in competition with a true provider of rural cellular service. The latter is not going to construct a chain of microwave stations at over a million dollars per station primarily to place cellular radios on them. Yet, unless the FCC gives some priority to those proposing to provide service along the federal interstate highway system, true nationwide cellular service will never occur. I believe that this Committee should determine whether the lottery is more in the public interest in such cases than a planned nationwide system.

STATEMENT OF WALTER G. BOLTER, PH.D., CPA, DIRECTOR,
BETHESDA RESEARCH INSTITUTE, LTD, ROCKVILLE, MD

Good afternoon, Bethesda Research Institute, Ltd. (BRI) welcomes this opportunity to present our views concerning the issue of cellular applicant eligibility in Rural Service Areas (RSA). As you may be aware, the Institute, as a member of the research community, conducts independent analyses and investigations in telecommunications and other industries, and often addresses major policy areas, specializing in matters related to economics, engineering, and finance.

My name is Walter G . Bolter. My current position is Director of BRI. I was formerly Chief Economist of the U. S. House of Representatives' Subcommittee on Telecommunications. Prior to that position, I served as Chief of the Economics Division of the FCC's Common Carrier Bureau and Senior Economist in the Department of Commerce's Office of Telecommunications. I have presented numerous papers and authored major monographs, reports or books, on telecommunications related matters. In addition, I have testified before the Congress, FCC, and numerous state and foreign regulatory, legislative, and judicial bodies.

It is my hope today that I may be able to utilize my experience in examining telecommunications policy issues from a public interest viewpoint at both the federal and state level to afford this Subcommittee some insights concerning resolution of the cellular RSA question. Specifically, I intend to address, from an economic perspective, the impact of limiting cellular applicants in rural areas to existing system operators, i.e., Metropolitan Statistical Area (MSA) companies and radio common carriers (RCCs). In particular, I will discuss the contrasting higher net benefits to society and efficacy of pursuing a much more open policy for entry into these rural markets.

★ ★ ★ ★ ★ ★ ★

The telecommunications environment has changed significantly over the past 30 years. For example, during the late 1950s this sector was characterized by, inter alia, few and similar services, analog networks, electromechanical equipment, pervasive regulations, and limited competition. However, with the onset of the computer and electronics revolution in the late 1950s and 1960s, the concomitant rapid technological change led to the introduction of diverse new services, digital electronic switching and transmission systems, and novel deregulatory and procompetition initiatives. A principal hallmark of this changeover was more open entry. This approach took hold especially where conflicts with other social objectives (such as maintenance of universal telephone service) were minimized or where technological imperatives (e.g., scale or scope economies did not appear to prevail.

At the federal level, a series of decisions adopted by the FCC and generally affirmed by the courts generally embraced easier entry and other competitive attributes as central features of public policy. Thus, in 1968, the FCC's Carterfone decision extended its earlier Hush-a-Phone findings by allowing the use of nontelephone company, or "foreign attachments" for telephone service, thereby permitting competitive entry in the customer premises equipment (CPE) market. And, in 1977, the Commission's Specialized Common Carrier decision opened the way for interexchange competition for AT&T and local exchange carriers, similarly, the FCC's 1972 Domestic Satellite, or "Domsat" ruling initiated an "open skies policy" for provision of satellite service.

Over the last decade, the agency's open entry policy stance was extended beyond its initial limitations to interconnection and specialized service areas. For instance, the Commission's "Part 68" registration program, begun in the mid-1970s, quickly set minimum technical quality standards for almost all major CPE, and reflected an attempt to prudently accommodate a variety of equipment suppliers.

The FCC's open entry initiatives took an even broader approach in the interexchange service area. First, in Docket 20003, the FCC determined in 1976 and again in 1980 that entry in interexchange markets was not economically harmful. Moreover, deregulatory policies implemented during the Commission's second and third computer inquiries (CI-2 and CI-3), "Competitive Carrier" proceeding (FCC Docket 79-252), and related cased recognized the salient effects of full open entry and competition

on the well-being of the ratepayer. Finally, the institution of the "equal access" program for interexchange carriers and inauguration of "comparably efficient interconnection" (CEI), as a precursor for "Open Network Architecture" (ONA), concerning information service access are examples of current Commission programs which are specifically directed at facilitating the presence of multiple vendors.

As in the case of the FCC, the courts have generally been supportive of multiple competitive entry in telecommunications. Appellate courts have generally backed the Commission in promoting such policies. And the key "Modification of Final Judgment," which set the terms for breaking up the Bell System to encourage competition, was sanctioned by Judge Harold Greene's District Court as an imprimatur on the principles of entry as highly beneficient social policy.

While slower to change, many state and foreign public authorities have also come to embrace pro entry policies in many instances in recent years. For example, most states currently allow interLATA interexchange competition within their respective borders, and some have allowed or will soon allow intrastate intraLATA toll competition. Alternative supply has even been permitted to a limited degree in local exchange markets in the form of private microwave systems, direct interconnection to toll carriers, private lines, and other bypass modes, including cellular radio. Canadian, Asian, and European authorities, to differing degrees, have also looked to more open entry to spur technological and service innovation in recent years, with the prospect of further liberalization on years to come.

Thus, open entry and equal access are cornerstones of public policy in most U.S. federal telecommunications markets and many states today. This approach is also taking hold world-wide. Whether the issue is accessibility to a market directly (e.g., receipt of a certificate of public convenience and necessity), or to a means to participate in a given market (such as applying for use of microwave frequency), government officials and the courts have consistently sought to remove barriers to such entry.

The approach set forth in the House Energy and Commerce Committee 's Report accompanying H.R. 2961, if implemented, stands in sharp contrast with development of what has become mainstream public policy. Limiting cellular radio applications for both wireline and nonwireline blocks (of frequency) in RSAs to existing licensees appears to be a highly imprudent initiative at a time when more--not less--accessibility is being much more generally embraced by policy makers the world over. Moreover, the proposal promotes concentration of market power, sanctions unreasonable discrimination, and is based upon assumptions which have no empirical basis or support.

As originally implemented for cellular markets, the FCC's program embraced for the first time dual facilities supply and permitted multiple services vendors in each of the designated markets. Diversity of ownership was achieved despite administrative obstacles. In a given market, a nonwireling ("A block) slot and a wireline ("B block") slot were authorized for facilities provision.

Notably, applications for the top 30 markets were accepted in 1982, and the first system (then AT&T'S AMPS, later known as Ameritech Mobile) became operational on October 13, 1983. These MSA companies were selected during comparative hearings held at the FCC. Subsequently, applicants were screened for financial and technical worthiness before the "winners" were chosen through a novel lottery process.

Of course, the initial level of concentration permitted by regulatory processes has been altered by intervening strategic developments over the past two years. Concentration of ownership has become pronounced. For example, during that period a trend has begun whereby several of the nation's principal nonwireline cellular operations have come increasingly under the control of wireline-based companies.

As a case in point, a Bell regional company, Pacific Telesis, purchased nonwireline cellular provider Communication Industries in 1986 for $432 million. Similarly, in 1987, Southwestern Bell Corp. acquired most of nonwireline Metromedia, Inc.'s mobile properties for $1.2 billion. The same year, BellSouth gained control of a cellular subsidiary of MCCA (ACC) and the latter's nonwireline operations in Los Angeles and Houston.

Overall, Bell companies are partners in nine of the "A block" systems in the top 12 U.S. cellular markets. Of the nine, eight have a controlling interest, i.e., are the managing partners of the nonwireline operations in these markets, and each is typically paired with another Bell subsidiary operating the areas wireline slot. Although no single Bell entity operates both the wireline and nonwireline systems in a given market, the highly significant Bell regional company presence in the U.S. cellular areas overall has been growing significantly.

Yet, surprisingly, not even a Bell regional company can claim the nation's largest market share. This structural position of highest concentration is occupied by McCaw Communications, which has been aggressively purchasing cellular entities during the past two years. McCaw operates in some 94 markets with potential customers exceeding 37 million. Other companies in the top 10 include affiliates of the 7 regional companies, GTE from 10.8 to 25.0 million.[1]. The regionals have even ventured into the overseas market. For instance, consider BellSouth International's joint venture with Air Call to provide cellular and paging services in the United Kingdom.

Price competition has been vigorous in many cellular markets because of resale and initial market rivalries. However, this activity will likely settle into nonprice rivalries and parallel pricing that are characteristic of tight oligopolies, both in theory and in practice. Examples of this conduct abound. Cereal and beer are two often-cited cases "classroom cases" although basic industries such as steel and vehicular manufacture have fallen into this mode. In telecommunications, the now more limited facilities providers in interexchange markets in this country now also appear to be evolving into this behavioral pattern.

---

[1]Statistical studies have demonstrated this relationship for a myriad of industries and sectors. For example, see the pioneering article by Joe Bain, "Relation of Profit Rate to Industry Concentration, American Manufacturing, 1936-40,"Quarterly Journal of Economics, 65 (August 1951), pp. 293-324. More recent significant works include, inter alia, M. Mann, "Seller Concentration, Barriers to Entry, and Rate of Return in 30 Industries", 1950-60, Review of Economics and Statistics, 48 (August 1966), p.296-307; L.W. Weiss, Quantitative Studies of Industrial organization" in M. intrilligator, Frontiers of Quantitative Economics (Amsterdam: North-Holland Publishing Company, 1971), pp.363-403; L. G. Shepherd, "The Elements of Market Structure," Review of Economics and Statistics, 54 (February 1972), pp. 25-38; P. D. Qualls, "Concentration, Barriers to Entry, and Long Run Economic Profit Margins," Journal of Industrial Economics (April 1972), pp.146-158; and S. A. Rhoades and J.M. Cleaver, "The Nature of the Concentration - Price/Cost Margin Relationships for 352 Manufacturing Industries: 1967." Southern Economic Journal (July 1973). pp.90-102. For usage surveys of these and numerous other studies supporting the basic high concentration - high profits linkage, see L. W. Weiss "The Concentration - Profits Relationship," in Industrial Concentration: The New Learning, edited by H. Goldschmid, M. Mann and F. Weston (Boston: Little Brown, 197j4) pp.196-201: and S. A. Rhoades, Staff Economic Studies, No. 92 (Board of Governors of the Federal Reserve System, 1977), "Updated, "Staff Economic Studies, No. 119 (Board of Governors of the Federal Reserve System, 1982).

Why should anyone care about such market characteristics as company share and pricing behavior? There is considerable support in the economic and policy community that both structure and conduct ultimately determine a market's performance in terms of bringing maximum service to consumers at least cost. Thus, such industry descriptors as seller concentration, entry barriers, and the degree on interdependence are more than likely to directly influence performance variables. Accordingly, high concentration and market power would presage excess profits reduced innovation and lessened operating efficiency than more rivalrous competition.

Indeed, empiricism has been developed by reserchers which shows, as expected that high concentration within a given market will be correlated with high profits.[2] In markets where the level of earnings is regulated, of course, such a relationship may not be permitted to occur. However, deregulation of many traditionally regulated sectors in telecommunications is increasingly commonplace.

Cellular is no exception. For instance, the Maryland Public Service Commission earlier this month recommended to the State's governor that the General Assembly repeal and eliminate the Public Service Commission's (PSC's) jurisdiction and authority to regulate the radio common carrier industry, including paging and cellular operations. And, even the FCC has recently announced its intention to eliminate the requirement for regional Bell companies to submit their cellular subsidiary capitalization plans for Commission review.

Clearly, a policy permitting existing cellular service providers to annex rural environs would only exacerbate the concentration problem that has arisen in this market. Instead of potentially unaffiliated duopolists in neighboring (MSA and RSA) market, the extent of the existing providers' market presence would expand. For example, the incumbent's 50 percent market share in a given metropolitan area could be broadened to a similar significant share in a geographic area that now included the outlying areas of suburbs. If the other incumbent failed to follow suit because of more attractive pursuits elsewhere, the first firm could establish a de facto monopoly as prospective entrants are barred from participation. If these providers are operation in a state where cellular telephony is deregulated, then the customers in the RSA might will be confronted by the specter of an unbridled monopolist.

It should be recognized that many of these incumbents are highly robust, financially well endowed firms which can trade on concomitant market presence in other telecommunications areas. For instance, as shown in the attached Chart, the Bell regionals represent 7 of the top 9 telecommunications firms ranked by their market value as of March 1986 and 1987. Market leader McCaw did lose $38.5 million in 1986, but this was because of large start-up costs. Indeed, McCaw's image on Wall Street is that of a "hot new stock" with bright prospects.[1]

In short, the Report's proposal can only serve to heighten market power in rural cellular markets. Incredibly, this comes at a time when supporters of deregulatory programs for this sector may be actually be gaining momentum.

Another fundamental drawback of the Report's approach is that it unjustifiably discriminates against prospective entrants. Yet, this discrimination does not draw upon any broad based evidence demonstrating that independent RSA companies are not as efficient or as technically capable as existing MSA providers and RCCs. Indeed, those entities awarded construction permits typically turn to the same contractors for engineering, installation, marketing and management

In fact, small remote switches, which would employed by entering firms, may actually be more cost effective that large urban switches utilized by MSA incumbents, since to utilize the MSA incumbent's "hub" arrangement, relays and repeaters must be used to transmit signals from distant rural sited. Moreover, the more localized operation of on-site independent RSA suppliers would likely result in a greater attention to introducing innovative equipment and offerings that urban-based companies focusing on their larger constituent base. Of course, universal standards developed by

Electronic Industries Association (EIA) would assure technical compatibility among the various cellular systems.

Financially, prospective cellular service providers would have to pass muster with the FCC, which requires a showing of a one year ability to build and operate a system. The track record appears promising. For instance, in excess of 70 percent of nonwireline MSA operators in October 1987 were not in business two years earlier, yet they obtained the funding that was needed to comply with the Commission's requirements.

The Report's recommended limitations would discriminate against some especially unlikely groups in the name of sound "public policy."

For instance, these would include minorities seeking ownership of cellular operations in rural areas. Also, those applicants who have already paid $200 initial application fees would be excluded. Ensuing lawsuits would clearly slow efforts to bring cellular services to RSA residents, hardly a result in the public interest.

Administratively, it cannot even be argued that the expected impact of an open entry approach on the FCC would, on balance, be negative. consider, for example, that the number of applicants for the less lucrative RSA markets is not likely to be comparatively large. Even if the turnouts were to be tremendous, computerization could keep the process manageable. Furthermore, the potential for a sizeable boost in application revenues would exist. This would accrue to the federal government at a time of significant budget deficits.

The only significant public concern about open accessibility to the cellular authorization process appears to be the threatened appearance of "get rich quick [1]applicants. Supposedly many of these entities, after being authorized to construct and/operate a system, will seek to barter the newly won license for a handsome remuneration.

To the extent that such behavior represents a real problem, there clearly exist the option of instituting requirements that would discourage such activity, while retaining an open entry framework. For instance, Congress could direct the FCC to establish a requirement that all RSA licensees cannot sell or promise to sell their licenses to others for a minimum of five years. This could be ordered in conjunction with mandatory showings of financial strength (e.g., the applicant's ability to build and operate a cellular system over a 3 year period, the usual gestation time for profitability to occur). Also, there could be required commensurate showings of technical prowess (such as equipment certifications, net relatively liquid assets of one half million dollars or at least $10 per constituent member of the RSA's population, and demonstration of in-house or outside qualifications to construct, engineer, market and manage a cellular system).

In conclusion, I believe that this Subcommittee should not endorse the proposed highly restrictive convenient on potential RSA cellular applicants. This poorly conceived preemption of open entry principles would, for the reasons discussed above, be substantially detrimental to a burgeoning market that occupies 75 percent of this country's geographic area and contains 60 million of its populace.

Thank you for permitting me to submit these comments today for the record. I would be pleased to answer any questions that you may wish to ask concerning this important issue .

POSITION PAPER

Representing the viewpoints of members of The American Cellular Engineering Association (ACEA) on the issues now pending before the Senate Subcommittee on Communication in its public hearing held on January 27, 1988:

1. **WE BELIEVE that every citizen of the United States who is financially, legally and technically qualified to apply for a Federal Communications Commission (FCC) Rural Service Area (RSA) cellular mobile telephone license should be allowed to do so without prior restraint.**

2. **WE BELIEVE that each person in America has the constitutional right to equal access and equal protection under the law and that this applies to open entry for participation in existing as well as new technologies. It also includes the right to compete freely and fairly for a license to operate a cellular mobile telephone system in metropolitan and rural areas of our great nation.**

3. **WE BELIEVE that the Congress and the FCC should fully enforce existing antitrafficking and non-transfer rules to prevent profiteering and trafficking in cellular mobile telephone licenses.**

   If present rules are not sufficient to prevent abuses, we further believe that a mechanism should be established to tax profits from quick sales or to impose rigid fines on those who violate these rules.

4. **WE BELIEVE that application fees for cellular mobile telephone licenses should be kept at a reasonable level to encourage new entrants to invest in this emerging industry and reserve their capital resources for the rapid construction of the cellular system.**

   High or restrictive application fees, in our opinion, should not be levied as a means to qualify applicants or limit trafficking in licenses. To enact such a fee structure would be to create an artificial barrier to entry and favor only the major corporate entities who could afford them. New business ventures must be afforded the opportunity to become established and be free from excessive fees during the start up years before these businesses begin to turn a profit. If a system of fees is to be imposed, we encourage the Congress and the FCC to consider a phased fee approach spread over several years AFTER the applicant has built the system.

5. **WE BELIEVE that the Congress and the FCC should encourage competition in telecommunications and not discourage it by establishing a negative precedent of sharply higher fees.**

   Several other technologies are about to be introduced in America, such as K-band satellites and high resolution television. If this high application fee precedent is set now for the cellular industry, it could also be followed for other new technologies.

6. **WE BELIEVE it is more economically and technically efficient to have new, rural cellular systems establish remote, standalone facilities than to piggyback on existing MSA switches or equipment.**

   Some have said it would be less costly and more expedient to use the adjacent MSA facilities to establish RSA service. We believe that the contrary is, in fact, the case. Large urban MSA switches can cost upward of $1 million and more each, while turnkey remote switches designed for rural applications can be purchased for $200,000 to $350,000. Furthermore, the cost of backhauling, or bringing back a signal from a remote region of an RSA to a MSA switch using microwave hops or terrestrial, landline facilities, is more expensive than utilizing standalone systems.

7. **WE BELIEVE it is unconstitutional to favor the existing MSA operators and to give them any preferential rights, treatment or exclusive access to the RSA application filing process--and thereby disenfranchise all others from exercising their free market right to compete for these licenses.**

Decisions of Federal District Courts and actions of the Department of Justice from 1956 through 1974 and culminating in 1984 have reaffirmed the concept of open entry in the telecommunications industry. During this time period, several antitrust actions were brought against AT&T resulting in the breakup of the Bell System. Charges included the concentration and abuse of monopoly power, among other suits. Since that time, the nation's leaders have repeatedly taken steps to ensure increased, not decreased, competition in the telecommunications industry while providing greater possibilities for entry as well as permitting a high degree of openness for new entrepreneurs.

8. **WE BELIEVE that separate coexistence between different MSA and RSA owner/operators is both possible as well as highly desirable and will result in faster development of rural cellular service in America.**

History has shown that when a new technology group (such as the cable T.V. industry, for example) which has been granted both rural and urban franchises, it usually invests more capital in building the inner-city business where higher population densities will yield a higher rate of return at the expense of developing the suburban and rural market segments. However, if these two markets are owned and operated separately, there will be high economic incentives for both entities to build their markets simultaneously.

9. **WE BELIEVE the Congress and the people of the United States do not wish to return to the monopoly/oligopoly era within the telecommunications industry which was prevalent for more than a century.**

However, to grant exclusive application filing rights to just a handful of large, vested cellular interests would be to reopen the door to the past and signal a return to the conditions which existed prior to the divestiture of the Bell Operating Companies from AT&T in 1984.

10. **WE BELIEVE that decentralized ownership of rural cellular mobile telephone licenses will stimulate industry growth and serve as a safeguard to attempts by those who wish to dominate this new technology and corner the market for themselves.**

More than 1,450 independent telephone companies have coexisted along side the dominant telecommunications carriers during the 100-year history of communications in our country. They have consistently provided quality service at reasonable rates to anyone in outlying areas who was willing to pay for service. These small, independent companies are a living example which proves the point that decentralization of ownership and control has worked well over the years. Furthermore, these firms are still capable today of carrying on this tradition of local provision of service while offering their customers the benefits of global communication access through a network of interconnecting links with the nationwide carriers. Should the country now turn away from this successful model as we enter the new age of cellular mobile telephone service or take a few lessons from the past?

IN SUMMARY, we believe that to deny any American the right to participate in cellular mobile telephony or any other technology would be a gross act of discrimination.

In a society founded on the principles of free enterprise, any law or regulation which tend to create artificial barriers would be viewed by the world as an act in restraint of trade. Can the United States send this kind of message to its own people, or much worse to its trading partners overseas. when it is actively seeking a lowering of trade barriers in the global economic community?

DBC COMMUNICATIONS, INC. Telecommunications and Broadcast Consultants
4401 East West Highway Suite 308 Bethesda MD 20814 (301) 654 0777

POSITION PAPER:

ADVANTAGE OF SINGLE RSA CELLULAR ENTREPRENEUR vs. MULTIMARKET SINGLE CELLULAR CARRIER -- A TECHNICAL PERSPECTIVE

Providing cellular radiotelephone service to Rural Service Areas (RSA) requires no technical wizardry. It does not require the entrepreneur who pursues a cellular license to posses an engineering degree or to have worked as a switch engineer with a telephone company. (Ironically, in the early days of cellular, large cellular market companies such as MCI, McCaw, PacTel, MCCA, etc., sought out telephone personnel to provide traffic engineering, switching, radio frequency (RF) engineering and AT&T cellular engineering expertise.) Thus, the inherent capability internal to these organizations in the early stages of cellular did not exist. It grew with time and the evolution of cellular.

In many cases, the engineer has been replaced by a business major and a marketing representative. If a problem arises, a cellular consultant or cellular vendor is called for a solution. However, the cellular entrepreneur must be technically, financially and legally qualified per Title 47, Part 22 of the Federal Communications Commission (FCC) Rules and Regulations.

Today, unlike yesterday during the infancy of cellular, enough mistakes have been made and enough solutions arrived at, that the new entrepreneur to cellular requires little technical foundation. The real need is capital and the desire to run a sophisticated radio frequency switching system with intelligence. It can be done inexpensively from a single cell (shared adjacent market switch) configuration to a little more expensive single cell stand alone switch configuration. In either case, the cost is under $500,000 dollars (assuming eight (8) channels and a small switch). Given this amount amortized over seven years at 11 percent interest would yield a monthly equipment expense cost of approximately $8,500 dollars. A number of entrepreneurs pay this amount in stagnant housing adventures, building purchases or stocks. They make money or lose money. It's the American way of life. A life that does not require college experience, a broker's license, law degree, engineering degree, business degree or a pedigree -- just plain desire and capital.

Capital is essential to any business adventure. However, in the cellular business much of the capital is available through vendor financing. Vendors, such as, Motorola, Plexys, NoVatel, to suggest a few, will provide financial assistance if the RSA market is economically sound. This is true simply because cellular is dynamic, untapped and growing. There are still 423 RSA markets that will represent 846 new market businesses.

Thousands of jobs and future RF engineering expertise will be derived due to the cellular entrepreneurial spirit of today. Limiting this spirit to the forged mentality of the few large carriers will destroy the creative nature of the new entrepreneur. New blood in any business causes movement. Some of the movement is good, some bad, however, movement of any kind wards off stagnation which is death in today's world of business and finance.

Will a multimarket single cellular carrier or existing RCC operator be able to provide better cellular service to an RSA than a new entrepreneur? No. Will the new entrepreneur make more mistakes today than the existing RCC or multimarket single cellular carrier did when the latter two started their communications businesses? No. Why? The new entrepreneur has available thousands of pages of information on cellular today that was not available when the older carrier started. Further, cellular vendors, especially for the small RSA markets, are eager to provide free advice and assistance. Before, they were still answering questions of their own, now these vendors can share their knowledge. In other words, the learning curve is not as steep for the new entrepreneur as it was several years back in the infancy of cellular. In addition, there are cellular consultants that have signficant experience which will allow them to guide the new cellular entrepreneur through the pitfalls that the earlier carriers encountered and stumbled upon.

The larger multimarket carrier represents to the industry what the large supermarket chains represent to the public -- retail cost reductions to the end user, due to volume. It only makes sense that the end user's product, the telephone, will cost less due to volume discounts obtained by the multimarket carriers. However, can the volume be maintained in order to receive these discounts as consumer buying levels off or declines due to technological change? As the large supermarket chains found out, the small markets could not substantiate the required level of consumer spending in order to survive. Thus, the large supermarkets had to pull out or cut back on the number of outlets. Ask the people on the East Coast what effect Safeway Stores, Inc., had on the public when they shut down their stores in the small markets. Jobs were lost and convenience was gone. The large chains need capital. The small market could not provide enough especially in a centralized, large business environment. Now the consumers are being served by the single owner, small-chain food stores.

This same scenario will be played out if single multimarket cellular carriers are given a free rein in RSA market entry. The larger markets will support the smaller markets such as the local exchanges supported the long distance toll rates under the old Bell System. Under that system the telephone company was seeking tariff increases yearly to support the capital hunger of their operations. New equipment, innovation and change was stagnate. Under the divestiture, we are seeing new digital services, faster information processing and good competition. This is because new blood forced good change in the telephone industry.

DB Communications, Inc. ---- 3

A single multimarket carrier or RCC will not serve the technical needs of the small RSA market any better than the new single market entrepreneur. The new entrepreneur will concern himself with the market he or she has been selected to serve. not a multiple number of markets.

The cellular vendor looks at the market potential for success prior to the selectee credentials in making financial assistance available. In selected MSAs, vendors came looking for selectees before the selectees went asking for help. The same will happen in the RSA markets.

Engineering a system for a small RSA market that is centrally located will be far less expensive than a large carrier trying to interconnect systems through large microwave "backbone" configurations. As a comparison, a small market with a small switch can be equipped for under $500,000 dollars. A small market with a single interconnected microwave loop will add an additional $150,000 dollars to this base cost. This adds 30% to the consumer cost unless a new way can be found to offset the additional expense. Being big is not less expensive... maybe more centralized or regionalized, but not less expensive. This additional cost must be passed on to the consumer or "eaten" by the carrier. Business dictates that the latter is not good business.

In closing, the FCC has long established the fact that to qualify for a communications facility an entity needs to be financially, technically and legally qualified per its established rules and regulations. The FCC does not look at existing or new carriers in any different manner if the above criteria has been met. Many financially, technically and legally qualified individuals have never filed for a cellular radio telephone facility or radio facility because they were not aware of the opportunity. Given their new awareness, it would be against the American Way to change the rules of entry that has stood since the existence of the FCC...legally, technically and financially qualified.

Signed,

Darrell E. Bauguess
President
D.B. Communications, Inc.

FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON

OFFICE OF
THE CHAIRMAN

DEC 22 1987

Honorable Daniel K. Inouye
Chairman, Subcommittee on Communications
United States Senate
SH-227, Hart Senate Office Building
Washington, D.C. 20510

Dear Chairman Inouye:

The Commission appreciates the Congressional concern about the filing of Cellular Radio Rural Service Area (RSA) applications by spectrum speculators. To that end, we look forward to participating in the Committee's January 1988 hearing on ways to discourage speculators from participating in that application process.

At the same time, the Commission is sensitive to the need to make cellular radio service available to all of the American people as soon as possible. Thus, as agreed upon by your staff prior to Senate adoption of the amendment precluding the FCC from accepting or granting any RSA applications prior to March 22, 1988, the Commission anticipates acting in January and February on several orders relevant to the RSA application process.

The matters the Commission expects to consider are: (1) a final order defining the ographic boundaries of the Rural Service Areas; (2) a final order on the RSA "fill-in" policy, i.e., how long RSA licensees will have to construct facilities in their area before the Commission will consider that area "unserved" and accept new applications to provide service for it; and (3) final action on the Commission's 1986 Further Notice of Proposed Rulemaking (Docket 85-388) in which the Commission proposed limitations on the formation of post filing settlement groups and the transferability of cellular radio applications as well as restrictions on the interests one entity may have in the RSA applications of another entity. Finally, the Commission may also determine the appropriate financial qualifications standards applicable to RSA applicants.

Further, as discussed and agreed upon by your staff, the Commission may issue an order in late February advising potential RSA applicants of the date on which it will accept RSA applications. Pursuant to the Administrative Procedures Act, an order of that nature must be issued 30 days prior to the day on which the Commission would actually accept RSA applications.

The Commission stands ready to work with the Congress as it analyzes whether legislation is needed to discourage speculators from participating in the RSA lottery process. Measures that have been suggested to us as possible solutions to the speculator problem include increased application filing fees or the charging of a grant fee. Under existing rules, all RSA applicants will be required to submit a $200 filing fee with their applications. Although it is not known what effect this filing fee will have on the number of applications filed, the information we have received informally indicates that the $200 fee will not cause a significant reduction in the number of filings. On the other hand, if the fee were significantly increased there is no doubt there would be a decrease in the number of speculative filings. As far as grant fees are concerned, we believe that imposition of a properly set fee, to be charged either when the construction permit is granted or when the facilities begin to serve the public, might also reduce the number of speculative filings.

In closing, let me reiterate that the Commission's goal is to make Cellular Radio Service available to all Americans as soon as possible. We have now granted all but approximately 40 of the 610 possible cellular MSA authorizations. Cellular Radio Service is a reality in virtually every major metropolitan area in the country. The acceptance and processing of the RSA applications as soon as possible will make this service available to all Americans not just those in the metropolitan areas. We look forward to working with you on this issue.

Sincerely,

Dennis R. Patrick
Chairman

NATELCO
ACRS
405/843-9986

National Telecommunications Companies, Inc.
Associated Communications & Research Services, Inc.
Harvey Parkway,
301 N.W. 63rd, Suite 225
Oklahoma City, Oklahoma 73116

Clayburn C. Curtis
President, ACRS

Dick R. Segress
President, NATELCO

January 27, 1988

The Honorable Senator Daniel K. Inouye
Hart Bldg.
2nd & C Street, N.E.
Washington, DC 20510

Dear Senator Inouye:

The Telephone Company owners of Associated Communications & Research Services, Inc. and National Telecommunications Companies, Inc. (ACRS/NATELCO) are concerned about several proposals which we understand Congress is considering in an effort to prevent the filing of speculative applications for licenses to provide cellular radio service in the rural service areas (RSAs) of the nation.

We represent local telephone companies serving 52 communities in Oklahoma. As such, we have an interest in being able to utilize cellular technology to bring improved and expanded communications services to our subscribers. We are, therefore, concerned about proposals to address the problem of speculative applications which may inadvertently harm our company, our subscribers and other potential cellular users throughout rural America.

Under the present Federal Communications Commission (FCC) Rules, two licenses for cellular service will be awarded to each RSA; one to a wireline applicant (a telephone company) and one to a non-wireline applicant. While wireline applicants would be limited to entities which are controlled by the telephone companies that serve the RSA, there is no such restriction on the non-wireline applicants. Further, there has been no assertion of any problem with regard to speculative applications for the wireline license. We understand that the proposals to address the problem of speculative applications are therefore intended to apply only to applications for the non-wireline license. These proposals include: (1) limiting the eligibility for a non-wireline RSA license to existing cellular licensees in adjacent metropolitan service areas (MSAs) and to radio common carriers (RCCs) that offer conventional mobile radio-telephone service; (2) increasing the license application fee from the present $200.00 to up to $25,000; and (3) charging a fee of $100,000 to $200,000 to the licensee when the operating license is granted.

Although these proposals have been made in the context of applying only to non-wireline applicants, we are concerned that adoption of any or all of these proposals will have adverse effects on small rural independent telephone companies and their subscribers. Historically, the FCC has endeavored to make fair and equitable decisions when applying their rules and regulations to competing parties. An attempt is made to apply the terms and conditions imposed for one class of service providers to all providers. Therefore, it is reasonable to expect that any exorbitant application and/or license fees applied to the non-wireline segment will, in fact, also be applied to the wireline segment. Since speculative wireline applications are not a problem, there appears to be no justification for increasing fees.

Equally important is the fact that fees at the level proposed could result in cellular service not being offered in rural America, where there is presently only marginal feasibility for its provision. At best, future rural cellular providers who pay these fees will inevitably recover them through the rates they charge their subscribers. We believe that it would be unjust for rural Americans to have to bear such costs when no similar fees were charged with respect to the provision of cellular service in the more economically lucrative metropolitan areas of the country.

We believe that there are rational alternatives to these proposals which more directly address the problem of speculative applications without posing the potential for harm to the independent telephone companies and their subscribers. For example, potential speculators could be discouraged by preventing the licensee from selling the license for profit until the cellular system has been constructed and operated for as long as necessary to effectively eliminate speculation.

We recognize that there is a problem with speculative non-wireline applications in the RSAs. However, the imposition of unreasonably large fees will impose a hardship on wireline applications which could jeopardize cellular service in rural areas. For this reason, we ask that you reject these proposals and consider an alternative, such as the one outlined above.

Sincerely,

Clayburn C. Curtis
President, ACRS, Inc.

CCC/lw

HOBBS, STRAUS, DEAN & WILDER
LAW OFFICES
1819 H STREET, N.W., SUITE 800
WASHINGTON, D.C. 20006
(202) 783-5100

CAROL L. BARBERO (DC)
S. BOBO DEAN (DC, NY)
HAROLD M. GROSS (DC, CA, OR)
CHARLES A. HOBBS (DC)
FRANCES L. HORN (DC, WV)
MARSHA KOSTURA (DC, PA)
MICHAEL L. ROY (DC, MA)
JOSEPH J. B. RYAN (DC, TX)
THEODORE A. SHIELDS (DC, MD)
JERRY C. STRAUS (DC)
LEROY W. WILDER (OR, DC, CA)

MIRIAM L. CHESSLIN (WA, NY, KS)
MICHAEL P. GROSS (NM, AZ)
KENNETH F. TWOROGER (DC, FL)
ROBERT H. WAGSTAFF (AK, KS)
OF COUNSEL

KAREN J. FUNK
GOVERNMENTAL AFFAIRS COORDINATOR
(NOT ADMITTED TO ANY BAR)

PORTLAND OFFICE:
1630 S.W. HARBOR WAY, #401
PORTLAND, OREGON 97205
(503) 242-0705

NEW MEXICO AFFILIATE:
ROTH, VAN KIMBERG, GROSS, AMARANT & ROGERS
P.O. BOX 1447
SANTA FE, NEW MEXICO 87501
(505) 988-8979 AND 983-7319

FLORIDA AFFILIATE:
TWOROGER & SADER
P.O. BOX 11506
FORT LAUDERDALE, FLORIDA 33339
(305) 565-8990

ALASKA AFFILIATE:
WAGSTAFF, POPE & CLOCKSIN
912 WEST SIXTH AVENUE
ANCHORAGE, ALASKA 99501
(907) 277-8611

January 27, 1988

Hon. Daniel K. Inouye, Chairman
Subcommittee on Communications
Committee on Commerce, Science
and Transportation
United States Senate
Washington, D.C. 20510

Re: Cellular Licensing

Dear Mr. Chairman:

We deeply appreciate the opportunity to submit the views of the Seminole Tribe of Florida in connection with the oversight hearing the Communications Subcommittee is holding with respect to cellular licensing. We believe we speak from a different perspective from those the Subcommittee has heard from before, yet one that has direct bearing on the purpose of the hearing.

We represent the Seminole Tribe of Indians of Florida. Our clients are well aware of, and very grateful for, your dedicated work as Chairman of the Select Committee on Indian Affairs and the strong commitment and knowledge you have demonstrated to tribal sovereignty and tribal economic development. We and they particularly appreciate your recent efforts to expedite handling and passage of the legislation settling the Seminole Tribe's land claims in Florida, now P.L. 100-228.

We write today to express our concern about the Federal Communications Commission (FCC) process for determining a procedure under which it proposes to award cellular licenses in Rural Statistical Areas (RSAs), insofar as they affect the

interests of the Seminole Tribe of Florida and other federally-recognized American Indian tribal governments with reservations in one or more RSAs.

Our main concern is that no consideration was given to the particular and special status and needs of Indian tribal governments within RSAs.

In its recent order, "In the Matter of the Commission's Rules for Rural Cellular Radio Service," released June 8, 1987, the FCC recounts that "We [the FCC] solicited comments from the public including state authorities on modifications to the United plan that would enhance the economic viability of rural cellular service." [Emphasis added.] (Par. 2.) No equivalent solicitation of tribal government views was sought.

The Seminole Tribe of Florida has four reservations within two RSAs (## 360, 361). These are Florida RSAs #1 and #2, respectively. The Seminole Tribe of Florida is the tribal sovereign government over 88,585 acres within these two RSAs.

As you know, federal policy is now to recognize and encourage the exercise of tribal self-government and the sovereignty of Indian tribes. Under P.L. 93-638, for example, various federal agencies are contracting out to willing tribes programs previously operated by the Bureau of Indian Affairs (BIA) or by the Indian Health Service (IHS). Recent changes in environmental laws recognize qualifying tribal governments as "states" for the purpose of clean-up planning and enforcement of, for example, the Clean Water Act and the Safe Drinking Water Act.

Under these legislative changes, tribal governments are administering their own schools, constructing and operating their own hospitals, running their own law enforcement agencies, and managing their own public water systems.

The Seminole Tribe of Florida -- as part of the land and water settlement with which you are familiar -- has created and is operating a tribal water office, regulating activity with respect to federal environmental laws and the equivalent of Florida water laws on its reservations, in cooperation with, but free of the administrative control of, the South Florida Water Management District, which regulates water use in the neighboring area.

Significant federal effort to encourage economic development on Indian reservations, not only with grants and loans, but with special set-asides and Indian preferences and priorities, is provided not only by the BIA in the Department of

the Interior, but by HUD, by HHS through the Indian Health Service and the Administration for Native Americans, and by EDA in the Department of Commerce.

However, in the very economically significant area of communications, according to the National Association of Broadcasters, Indians are virtually unrepresented. There are only 16 Indian-owned radio and television stations in the country, 13/100's of one percent. To our knowledge, there are at most a handful of other kinds of Indian-owned communications facilities. In fact, the FCC seems unaware of the existence of tribal governments, and not only overlooks but effectively restricts the opportunities for tribal economic development by rewarding those who ignore tribal sovereign rights.

Specifically with respect to the question before the Subcommittee -- the procedures for awarding cellular licenses -- the FCC, by not taking into account the special position and needs of tribal governments in RSAs, gives special privilege to telephone companies which have often ignored the sovereignty of tribes, and, under the FCC system, have an unfair advantage in the rounds of competition for licenses to operate cellular systems around, over and even within Indian reservations. This is done without input from the affected tribal governments and without sensitivity to the needs of the tribes these governments represent.

The economic window of opportunity to win a cellular license will be open for a limited time. Once these licenses are awarded, the same opportunity may never again exist. Yet, half of the licenses -- those in Block B -- will be reserved for competition among "wireline", that is, telephone companies.

That fact poses two problems for Indian tribal governments interested in insuring that their public is properly served by the system that is eventually adopted, and interested in participating in the opportunity for tribal economic development that exists here.

The first problem is illustrated clearly by the history of telephone service on Indian reservations. Typically, even now, what little telephone service exists is furnished by one or more telephone companies who happen to be operating in areas near the reservation. Telephone companies have often entered Indian reservations without the permission of the tribal government (though possibly with the acquiescence of federal officials), sunk their poles on tribal lands and strung their wires as their own convenience dictated, without regard for either the service needs of the tribal community or the planned uses for the land that a tribe might have. Telephone service to

remote parts of the reservation -- where it is often most necessary -- is often totally unavailable. And the overall quality of service is frequently very poor. Public convenience and necessity considerations are absent because the regulatory jurisdiction of state authorities stops at the reservation border and the phone company is not particularly responsive to the tribal government.

As a result, it is not unprecedented for a tribe to decide to take over and operate its own telephone service.

The Papago Tribe of Arizona purchased and now owns and operates its own local exchange company (LEC). The previous system, owned by Mountain Bell, had only 400 access lines to serve a tribal population of over 6,000 people on a reservation of 5,000 square miles. Many locations in more remote reservation areas have no telephone service. The present system is operated by the Papago Tribal Utility Authority. It is not subject to state regulation, although the State Corporation Commission cooperated in establishing the Authority. The Tribal Authority follows the Commission's rules for the sake of uniformity of service, but is not bound by them. The Tribe purchased the system from Mountain Bell with its own funds. The system is now undergoing a $7 million expansion, assisted by REA funding, which will enable the tribe to provide telephone service to all areas of the reservation.

Another tribally-owned LEC is operated by the Cheyenne River Sioux Tribe Telephone Authority in South Dakota. The system was created by the gradual purchase by the Tribe of a number of small switcher companies. As a result, this system provides both on- and off-reservation service. Again, it is not regulated by the state PUC.

The Seminole Tribe of Florida, one of a number of rapidly developing Indian Tribes, has decided that the best way to serve the tribal Community is to form and operate the Seminole Telephone Company, Inc.

The desire for greater tribal control over telecommunications activities on tribal lands is totally consistent with the tribe's efforts, encouraged by federal policy, for tribal self-government and the pursuit of economic opportunities for the Seminole Indians. In addition to plans for the operation of a local LEC for the four Seminole reservations, the tribe has a significant interest in pursuing the pertinent cellular wireline rights that accompany the status of an LEC. Therein lies the second problem.

Were the Seminoles in the position of the Papagos or Cheyenne River Sioux, there would be no question of their privileged standing as a wireline company to compete for Block B allocations for cellular licensing. Given, however, their standing on the threshold of creating a telephone company, while faced with an arbitrary time-constrained window of opportunity for obtaining a cellular license -- created by the FCC without the needs, interests or views of the tribal government in mind -- the Seminoles are properly concerned that by the time they have an operating wireline company, their opportunity to participate in the competition for cellular licenses will have been irrevocably lost. Moreover, there is reason to believe that there are at least a few other Indian tribes at a similar stage of their economic and governmental development and faced with a similar dilemma.

Indian tribal economic development is difficult enough without burdening their enterprises with handicaps that their economic predecessors and competitors do not have. In this case, it is the wholly arbitrary time window which could result in the Seminole Telephone Company, now in its formative stages, becoming operational, but then hampered forever by missing the opportunity enjoyed by all other phone companies to participate in the Block B competition for a cellular license.

For this reason, the tribe seeks legislation to insure that a federally-recognized Indian tribal government with one or more reservations within an RSA be treated as a wireline company for the purposes of the cellular licensing competition within that RSA.

We would be happy to discuss with you and the subcommittee any limiting language the subcommittee believes is needed to prevent potential abuse of this provision.

We would be delighted to discuss this important idea with you at your convenience, and hope this letter can be included in the record of your hearing.

Cordially,

HOBBS, STRAUS, DEAN & WILDER

By: Harold M. Gross
(Attorney for the Seminole
Tribe of Florida)

/sec

☆☆☆ American SMR Network Association, Inc.

February 12, 1988

The Honorable Daniel K. Inouye
Chairman, Subcommittee on Communications
Senate Committee on Commerce,
Science and Transportation
Room 508
Dirksen Senate Office Building
Washington, DC 20510-6125

Re: January 27, 1988 Hearing on
Rural Cellular Non-Wireline Licensing

Dear Senator Inouye:

Pursuant to the invitation extended during the above referenced January 27, 1988, hearing, the American SMR Network Association, Inc. (ASNA) is pleased to provide you with its views concerning rural cellular non-wireline licensing. ASNA strongly believes that any attempt to limit the categories of entities eligible to obtain rural cellular authorizations to those already providing common carrier service in adjacent communities is not in the best interest of the American public. Instead, ASNA believes, with the Federal Communications Commission, that in order to eliminate the submission of applications by those who do not intend to offer cellular service and thereby expedite the licensing process, Congress should authorize the FCC to increase application filing fees, impose substantial grant fees, or otherwise tighten financial qualification standards.

ASNA is a nationwide, non-profit trade association whose voting membership is comprised exclusively of Specialized Mobile Radio (SMR) licensees. ASNA's members operate primarily trunked SMR facilities offering two-way dispatch communications in urban, suburban and many rural markets throughout the country. These licensees offer a private, as opposed to a common, carrier service to tens of thousands of dispatch customers throughout the nation. Most offer mobile radiotelephone service interconnected into the landline telephone network as well. Because its members have become the premier providers of private dispatch communications, ASNA has a strong interest in the regulation of what it considers to be the complementary mobile telephone marketplace.

ASNA agrees that action is required to eliminate the substantial number of speculative applications that are submitted when the Commission wishes to offer a new service or existing services to new areas. Regrettably, ASNA members are familiar with the avalanche of "insincere" applications that are submitted when the Commission provides an opportunity for new entrants in the marketplace. In late 1986 and 1987, the Commission made available 900 MHz spectrum for SMR use by 20 licensees in our top 50 major metropolitan areas. In response to that invitation, the Commission received thousands of applications for the authorizations available in each market. The following is a listing of the number of applications filed for the top five metropolitan areas:

Metropolitan Area	Number of Applications
New York	4,675
Los Angeles	4,547
Chicago	2,613
San Francisco/Sacramento	2,318
Philadelphia	2,058

Even in less populated areas, where the availability of 800 MHz spectrum permitted open entry to the SMR market, hundreds of applications were submitted for the 20 available 900 MHz licenses.

ASNA agrees that the Commission or Congress must act to prevent the submission of applications by entities proposing to serve areas where they clearly do not have an intention to offer service. However, any proposal to eliminate an applicant's eligibility merely because it is not already providing a common carrier service in an adjacent community is unnecessarily anti-competitive. Moreover, the presumptions on which these proposals are based are fundamentally flawed. In his testimony, Mr. Thomas Stroup of the Telocator Network of American (TNA) stated that:

> "Most rural cellular systems are logical extensions of either the cellular systems serving the adjacent metropolitan areas or the operations of radio common carriers already licensed in rural areas to provide conventional mobile telephone service. Cellular and mobile telephone operators are already familiar with the technical and marketing needs of the community. They are experienced businessmen and businesswomen who can deliver service to the public simply by extending their existing systems - either geographically or by adding new technology - to cover rural areas. Moreover, they could begin offering service quickly and with less expense than having to build new systems from scratch."

These precise qualifications apply to operators of SMR facilities as well. They too are third party providers of two way telecommunication services in the markets where rural cellular systems will soon be built. They also are familiar with the technical and marketing needs of those rural communities. If, therefore, Congress intends to limit entry to the rural cellular marketplace, SMR operators should also be considered in the category of eligibles who are permitted to submit applications to offer the service.

Nevertheless, the preferred method to discourage speculators both in the cellular and SMR industry is to erect more substantial financial barriers against the submission of purely speculative applications. This is the approach favored by the Federal Communications Commission and the Cellular Telecommunications Industry Association (CTIA) in their testimony before the Subcommittee. CTIA specifically recommends that applicants demonstrate their financial qualifications either by:

1) placing in an escrow account one third of all system equipment costs and the costs of all operations for one year, or

2) obtaining a letter of credit for those costs.

Regardless of the precise nature of the financial demonstration required, ASNA strongly agrees that more stringent financial qualifications should remain the only barrier to entry for rural cellular applicants. A system which provides a preference among applicants for a new service to those already entrenched in the same industry contravenes the public interest, and more basically, any sense of fair play.

ASNA appreciates this opportunity to express its views to the Subcommittee. Should there be any questions, please feel free to contact me.

Cordially yours,

Russell H. Fox
Executive Director

LAW OFFICES
KOTEEN & NAFTALIN
1150 CONNECTICUT AVENUE
WASHINGTON, D.C. 20036

BERNARD KOTEEN
ALAN Y. NAFTALIN
RAINER K. KRAUS
ARTHUR B. GOODKIND
GEORGE Y. WHEELER
HERBERT D. MILLER, JR.
MARGOT SMILEY HUMPHREY
PETER M. CONNOLLY
CHARLES R. NAFTALIN

TELEPHONE
(202) 467-5700
TELECOPY
(202) 467-5915
CABLE ADDRESS
"KOBURT"

February 12, 1988

Senator Daniel Inouye, Chairman
Senate Sub-Committee on Communications
U.S. Senate
508 Dirksen Building
Washington, DC 20510

Dear Senator Inouye:

On behalf of Telephone and Data Systems, Inc. ("TDS") and United States Cellular Corporation ("USCC") this will comment on the issue of eligibility to apply to serve Rural Service Areas ("RSA") in the Domestic Public Cellular Radio Telephone Service, concerning which the Sub-Committee held hearings on January 27, 1988. We further request these comments be made part of the hearing record.

TDS is a Chicago-based holding company principally engaged in the business of acquiring and operating telephone and other companies, primarily in the communications industry. As of December 3, 1987, TDS had an interest in 71 telephone companies located in 24 states. TDS subsidiaries now also operate 94 mobile telephone and/or paging systems in 32 states and the District of Columbia.

USCC, which is 93.8% owned by TDS, owns, operates and invests in cellular systems in 62 cities in 25 states, holding majority interests in various wireline systems, including those in Tulsa, Oklahoma, Knoxville, Tennessee, and Asheville, North Carolina and in the non-wireline systems in Evansville, Indiana and Poughkeepsie, New York. USCC is actively engaged in acquiring additional cellular interests and plans to apply to serve RSAs wherever it is eligible to do so.

Thus, TDS and USCC have a substantial interest in the issue of RSA application eligibility and now respectfully request that their views on this issue be considered and included in the Sub-Committee's hearing record.

Under current FCC rules, wireline telephone companies and their affiliates may acquire controlling interests in non-wireline cellular systems subsequent to their authorizations by the FCC. USCC and other similarly situated companies have purchased such controlling interests in non-wireline cellular licensees and permittees.

TDS and USCC take no position in this letter on whether the Congress should act to limit eligibility to file applications to provide cellular service on non-wireline (Block A) frequencies to entities holding licenses, in or one more adjacent RSAs and to "radio common carriers" providing service in the RSAs, as some parties testifying at the hearing have proposed.

However, the "adjacency" and "radio common carrier" proposals discussed at the hearing would be unfair to TDS, USCC and similarly situated "wireline" companies holding non-wireline cellular licenses, unless Congress revises the proposal in the following respects to ensure fairness to all parties concerned.

First, Congress should require that <u>all</u> MSA non-wireline licensees be eligible to file for adjacent RSAs. Under current Section 22.902(b) of the FCC's Rules (47 C.F.R. Section 22.902(b)), only "common carriers not also engaged in the business of affording public landline message telephone service" may apply to provide cellular service on the "non-wireline" (Block A) cellular frequencies. However, subsequent to authorization, common carriers also engaged in providing telephone service may acquire non-wireline systems, and this has happened frequently. Thus, if an "adjacency" rule were adopted and existing FCC Rule 22.902(b) were left in place, the non-wireline licensee in a given MSA would not be eligible to apply initially to serve a neighboring RSA if it were affiliated with a telephone company anywhere in the United States. This we would consider to be contrary to the public interest in the best possible cellular service and unfair to such licensees. If, as the proponents of the rule argue, the public interest in efficiency and economy of service is promoted by the rule, that is equally true whether or not the MSA non-wireline licensee is a wireline affiliate. If an "adjacency" rule is adopted, Section 22.902(b) should be modified to allow all MSA non-wireline licensees to file for the non-wireline authorization in neighboring RSAs, subject, of course, to the rule that no applicant can file more than one application in a given RSA. If an applicant were eligible to file for both the wireline and non-wireline frequencies, it would have to make an election.

Second, and similarly, if the Congress chooses to limit the applicants eligible to apply for non-wireline RSA frequencies to "radio common carriers" within the RSA it should ensure that the definition of "radio common carrier" now found at Section 22.2 of the FCC's Rules (47 C.F.R. 22.2) is not used to determine eligibility. The FCC presently defines a "radio common carrier" as a "common carrier" engaged in the provision of Public Mobile Service which is not also in the business of providing landline local exchange telephone service. Here again, if the FCC definition were applied, a common carrier providing paging or mobile telephone service in an RSA which was affiliated with a telephone company anywhere in the United States could not apply to provide non-wireline cellular service in the RSA. This outcome would not serve the public interest, which is in obtaining the best possible proposals for service in the RSAs and again would be unfair to those companies which could not apply. Again, however, if the rule were modified to allow radio common carriers under common ownership with telephone companies to apply for the non-wireline frequencies in RSAs, no applicant would be able to file more than one application in any given RSA even if it were otherwise eligible to apply for the wireline and non-wireline frequencies.

TDS and USCC believe that if any "adjacency" rule is applied that these revisions in the rules are essential to ensuring the "level playing field" for all applicants which we know that the Congress desires to achieve.

Very truly yours,

Alan Y. Naftalin

Alan Y. Naftalin
Counsel to Telephone and Data Systems, Inc. and United States Cellular Corporation

MOBILCOM
MOBILE COMMUNICATION SERVICE
P.O. BOX 1234 MEADVILLE, PENNSYLVANIA 16335 PHONE (814) 724-1234

John

Clare A. Watson, *President*
Denny P. Watson, *Vice President*

NATIONAL MOTOROLA Communications SERVICE

January 12, 1988

The Honorable Daniel K. Inouye
722 Hart Senate Office Bldg.
United States Senate
Washington, D.C. 20510

Dear Senator Inouye,

Mobilcom is a supplier of mobile telephone service, serving 10,000 square miles of northwestern Pennsylvania. We have been providing these services since the early sixties. We serve primarily rural territory. The Federal Communications Commission will soon be accepting applications for cellular telephone service for the rural area we serve.

As currently proposed, the Commission will grant cellular licenses by lottery unless Congress takes action to stop this injustice. If left uncorrected, the lottery process will lure in thousands of applications based upon the "application factory's" claim that the winner will obtain instant wealth. There is no desire or intent of the speculators to build and construct a cellular system to meet the needs of the area.

Investors, or should we call them more realistically - gamblers, are being lured by promoters who don't inform them that there is only a remote chance of success in the lottery. I have personally received calls from these application factories and have heard their pitch. They push the untested theory that if you apply for every RSA in the county, you are virtually assured of success.

The proposed lottery is a windfall for those opportunists who chose to make an industry out of the Commission's desire to expedite the delivery of service to the public and keep the cost of entry from being prohibitive. In the end, the Commission's intent is scuttled as well, because the "winner" of the lottery is not prepared to build a cellular system. The typical winner begins his search for a buyer. The Commission's desire for expediency and economy have both been immediately subverted.

Perhaps the worst part of this scenario is the fact that the "winner" of the RSA lottery will be winning commodity which has never before existed and for which there is no established value. To have "won" a lottery for an RSA serving some 201,000 people in three counties, totalling 2,611 square miles, such as is the case here in my home RSA, Market #610 - PA RSA#1, is a completely different economic situation than to have been awarded the cellular license for MSA #130, Erie, PA with a population base of 280,000, residing in an area of 810 square miles, which is currently being served by one cellular site. The RSA "winners" may not be capable of building or selling their cellular licenses. Will a new "industry" be created by the now defunct application factories to take care of buying, selling and swapping of RSA licenses? At this stage, what will have happened to the Commission's good intentions?

I don't believe it was the intention of the Commission, but in this process, those of us who created and built the existing mobile telephone industry have been relegated to the same level as some obscure speculator who has never seen nor heard of PA RSA #1. Those with proven expertise in providing quality service who for decades asked for more spectrum to better serve their subscribers are now outsiders looking in.

I have read every word I could get my hands on these last few years about the potential for cellular in rural America, It is not going to be easy to produce profits. But if it can be done, it seems that those who have the skills, commitment and capacity to serve the public should be the ones to whom the Commission looks to do so.

I understand that the Senate Commerce Committee will be holding hearings soon to consider these issues. I believe that only those who have the natural incentive to provide the lowest cost, most technically efficient service, and who have already demonstrated their ability to serve the public, should be allowed to compete for rural cellular licenses.

Gambling with rural cellular service will hurt many more Americans than it will help. Tens of thousands of innocent investors will be tempted to take a remote gamble. And if these speculators win, they will only add cost and delay to the provision of cellular service to our rural areas. Please support legislation to end this abuse of the lottery process, and to ensure that rural America gets quality cellular service at competitive prices from people who have demonstrated their ability to provide such services. Competition for cellular licenses should be among those currently providing conventional mobile telephone service to the respective RSA.

Please let me know your thoughts on this matter. I am available by telephone at 814-724-1234. If you need anything further from my perspective, please ask. Thanks for your interest.

Very truly yours,

Denny R. Watson

LAKEDALE TELEPHONE COMPANY

ANNANDALE, MINNESOTA 55302

AREA CODE 612

TELEPHONE 274-8201

January 26, 1988

Senator Daniel K. Inouye
Chair, Senate Subcommittee on Communications
722 Hart Building
2nd and C Streets, Northeast
Washington, D. C. 20510

Dear Senator Daniel Inouye,

I am writing this letter, to express an opinion, as the President of the Minnesota Telephone Association and on behalf of its Board of Directors.

We have been monitoring the cellular issues before the Federal Communications Commission as closely as possible. In Minnesota the Association has formed a cellular committee and this has been their responsibility to monitor the efforts and actions of the Federal Communications Commission and also bring the telephone companies here in Minnesota to a level of awareness, where they can participate in the cellular business as we know it today. The companies in Minnesota are certainly involved in the process and presently 84 of our companies are going to be filing for the cellular license as soon as is humanly possible.

Our committee has recommended to our Board of Directors, that we take a position to oppose any legislation that would provide an unfair advantage for any large company over a small company, because here in Minnesota this would discourage competition and may ultimately prevent some of our local rural citizens from receiving cellular service. We realize that many of the proposals are presently being directed at the non-wireline or non-telephone company providers. However, in many cases these issues could involve the telephone companies or the wireline providers and we would be in opposition to this.

Our major concerns are:

1) The proposed large licensing fees or unreasonably high bank lines of credit.
2) We oppose changing the current liability requirements for the Rural Service Areas, because the current proposals would prohibit rural minority license holders in the Metropolitan Statistical Areas from serving the adjacent the Rural Service Areas and this does not make good economic sense in our opinion.
3) We support the applications of the rules as they have been so stated previously in the Metropolitan Service Areas, which we feel would encourage fair and equitable procedures in issuing Rural Service Area licenses.

If you have any questions or would like any further correspondence regarding our position in this particular issue, please do not hesitate to contact me accordingly.

Sincerely,

Bud L. Morrow
President

National Telephone Cooperative Association

2626 Pennsylvania Ave. N.W.
Washington, D.C. 20037
(202) 298-2300

February 11, 1988

The Honorable Daniel K. Inouye
Chairman, Subcommittee on
Communications
Senate Committee on Commerce, Science
and Transportation
227 Hart Senate Office Building
Washington, D. C. 20510

Dear Chairman Inouye:

On behalf of the National Telephone Cooperative Association (NTCA), I am submitting this statement for the record for the January 27, 1988 hearing on rural cellular licensing.

The National Telephone Cooperative Association (NTCA) is a national trade association which represents more than 450 small, independent cooperative and commercial telephone systems throughout rural America. We serve millions of subscribers in some of the most high-cost, sparsely populated areas of the nation.

NTCA members and their subscribers have been waiting several years for cellular service to come to rural America. The Federal Communications Commission (FCC) has completed the licensing process in the Metropolitan Service Areas (MSAs) and is now ready to begin licensing the 423 rural service areas (RSAs). Some industry groups are now raising the issue of excessive license speculation for RSAs and have proposed that "corrective" legislation be enacted before licenses are awarded. While NTCA recognizes that speculation has been a problem in the MSA nonwireline licensing process, the legislative process and subsequent rulemaking could delay cellular service to rural Americans.

Changing the rules governing the issuance of nonwireline cellular licenses in RSAs would be unfair and would discriminate against rural cellular providers and their customers. For example, drastic changes in the eligibility requirements for applicants, as proposed by some, could disqualify parties who are genuinely interested in providing service. Imposing exorbitant licensing fees on RSAs but not MSAs is inequitable, puts a financial burden on providing service to areas that have questionable profitability, and could result in fewer service providers to rural areas.

To solve this problem expeditiously, the Senate Commerce Committee should set cellular telecommunications policy and charge the Commission with the responsibility of promulgating rules to implement that policy. To that end, the committee should tell the FCC it is opposed to flagrant license speculation and request that the Commission take steps to fine-tune its rules in an effort to respond to Congress and reduce speculation.

The FCC has recognized that there is a problem with speculation among nonwireline cellular applicants and it is making additional regulatory improvements which will help alleviate the problem. Improvements include prohibiting speculative alliances, strengthening the financial showing requirements and carefully scrutinizing requests for license transfers.

NTCA also suggests that the Commission consider reinstating the pre-screening rules that were used in MSA markets 91-120 in an effort to stem speculative applications. To accommodate increased administrative costs caused by pre-screening and other regulatory improvements, the Commission could make an adjustment in the application fee.

There is no easy solution to the speculation problem and there is no consensus in Congress or in the industry as to what should be done. Legislation will only delay cellular service to rural areas and delay is worse than speculation. Rather than pursue a legislative solution to this problem, we feel that it is appropriate for the Commerce Committee to establish a policy of opposition to excessive license speculation. The Committee should then provide the necessary oversight of FCC activities to insure that this policy is carried out.

Thank you for the opportunity to provide the Subcommittee with our views on this important issue.

Sincerely,

Mike Brunner

Michael E. Brunner
Executive Vice President

LAW OFFICES
GORDON & HEALY
CHARTERED
1821 JEFFERSON PLACE, N.W.
WASHINGTON, D.C. 20036
(202) 785-8020

HAROLD GORDON
ROBERT W. HEALY
ROBERT D. ROADMAN

TELECOPIER
(202) 223-7281

January 26, 1988

Honorable Daniel K. Inouye
Chairman, Communications Subcommittee of the
Senate Committee on Commerce, Science, and Transportation
c/o John Windhauser
Hart Senate Office Building
Room 227
Washington, D.C. 20510

RE: Lottery Award of Rural Service Area Cellular Authority (RSA)

Dear Senator Inouye:

In regard to your Committee's concerns about the prompt institution of RSA service, without the impediment of spectrum speculators, I would like to submit the attached testimony of Mr. George M. Batsche, President of Communications Transmission, Inc. Since that testimony speaks for itself, I thought, that without repeating that testimony, I would briefly explain why I believe it to be relevant to your Committee's concerns.

That Americans living in rural areas must not be deprived of new communications technology presently available to residents of metropolitan areas is, obviously, a matter of grave concern. However, we believe that the Committee should also be concerned about the inability of truckers, etc., on the federal interstate highway system to have available to them a nationwide cellular service.

There are number of larger interexchange common carriers (IXC's) who have built microwave systems connecting the major metropolitan areas. Coincidently, these systems often traverse the federal interstate highway system with towers located on an average of every twenty miles. As such, as Mr. Batsche testifies, they would be in an ideal position to create a continental cellular system capable of handling traffic along the interstates. However, under the FCC's lottery rules--since they are not local exchange carriers--their applications would be put into the same lottery bin as an applicant preparing

GORDON & HEALY
CHARTERED

Honorable Daniel K. Inouye
January 26, 1988
Page Two

to provide one cell anywhere within the entire RSA. For this reason, it is presently considered to be largely a waste of time and money for the IXC's to pursue providing an interstate highway interconnecting cellular service.

Perhaps if your Committee came to the conclusion that the present lottery system created an unnecessary obstacle to the development of a potential interstate highway cellular service this might be the opportune time for you to discuss with the FCC's representative how to overcome this obstacle. Cellular service would be far more attractive nationwide, if it were available not only in the cities, but also along the highways that connect those cities.

Very truly yours,

GORDON & HEALY, Chartered

By Robert W. Healy
Robert W. Healy

CELLTEK

1216 CAPITAL TOWERS BUILDING
125 SOUTH CONGRESS STREET
JACKSON, MS 39201

(601) 352 8625

January 20, 1988

The Honorable Daniel K. Inouye
United States Senate
722 Senate Hart Office Building
Washington, D.C. 20510

Dear Senator Inouye:

I would like to express my views on the pending review and hearing concerning the FCC's licensing procedure for the RSA cellular markets.

I represent a group of investors who would like to provide cellular telephone service to the rural areas. We would prefer to provide this service in Mississippi or one of our neighboring states but we realize under a lottery type of program that we cannot choose our locations.

We are prepared to file in almost all of the available RSA markets and would strongly oppose any legislation that would prevent us from doing so. While we may not be able to compete against the large phone companies in purchasing a license from a lottery winner, we can afford to file and develop a market that we win and would probably be providing the service years in advance of some of the larger companies.

I am aware of the concerns of some members of Congress concerning the abuse of the lottery systems, but I can think of a number of ways to curtail that abuse and still continue with the lottery system.

I plan to be in Washington D.C. next week and will attend the hearing scheduled for 9:00 a.m. on January 27 in the Russell Office Building, Room 253. I would like to have my letter made a part of the official record of this particular hearing.

Further delays to this system will only discourage the rapid development of this service to the rest of the country.

Sincerely yours,

Michael T. Guthrie

HCTC
HONOLULU CELLULAR TELEPHONE COMPANY

1181 Kapiolani Boulevard
Honolulu, Hawaii 96814
Telephone (808) 545-4755
Fax (808) 537-1512

January 22, 1988

The Honorable Daniel K. Inouye
722 Hart Senate Office Building
Washington, D.C. 20517

Dear Senator Daniel K. Inouye:

With the upcoming hearing before the Senate Commerce, Science and Transportation Committee on January 27, the residents of the outer islands stand before a critical juncture which will determine irrevocably the means, costs, and timing of the provision of cellular service in the Rural Service Areas (RSA's) here in Hawaii.

As President and General Manager of the larger of the two cellular carriers on Oahu, I would like to express Honolulu Cellular Telephone Company's opinion of how we can most quickly bring this much-asked-for service to the residents of the outer islands. Even among our existing customers on Oahu, many have asked about service on the outer islands since many contractors, tourist industry people, and business people constantly fly back and forth between islands. We also get numerous calls from the outer islands asking us about the availability of cellular service, which would make the provision of goods and services much more efficient.

On Oahu alone these are an estimated 3,500 plus users of cellular service on both Honolulu Cellular and GTE Mobilnet, users who have greatly benefitted from the productivity-raising nature of instantaneous and reliable communications. This growth has occurred in the short 18 months after the initiation of cellular service on Oahu by Honolulu Cellular.

In 1987 Honolulu Cellular's revenues for service and telephones were approximately $6.3 million, which gives one a partial indication of the value consumers see in this fast-growing technology. Since its inception, Honolulu Cellular has spent roughly $17 million on capital and expense items and now employs approximately 60 employees. There are also dozens of other agents of ours such as Motorola, Electronic Entertainment, Delta Mobile Communications and Service, who sell and service telephones for customers who use our system.

The FCC will this year accept these applications based on division of the outer islands into three RSA's: Kauai, Maui, Molokai, and Lanai, and the Big Island. We at Honolulu Cellular see some problems in bringing service to the three counties as quickly and efficiently as possible.

Background to Current FCC Rules

Today the FCC mandates two licensees or carriers of cellular service in every market in the United States. One license is limited to applicants from the telephone company or telephone companies which serve that market. The other carrier's license is open to all other applicants. The licenses of the largest markets or Metropolitan Statistical Areas (MSA's) have been generally awarded to Radio Common Carriers (RCC's), which are private mobile telephone, two-way radio and paging companies who offer service to consumers. Many of these RCC's have formed partnerships in the largest markets to speed the implementation of cellular service in order to compete against the telephone companies, who in some areas, such as Honolulu, had no competing applicants and thus received the license automatically. In the Honolulu market GTE Mobilnet, our competitor, received their construction permit from the FCC about a year before Honolulu Cellular. Honolulu Cellular, being a partnership of RCC's unique to Oahu, brought cellular service to Hawaii four months before its competitor, even though Honolulu Cellular had no existing organization (such as Hawaiian Telephone) to perform many of the support functions essential to building a large, new business. This speed in moving forward Honolulu Cellular attributes to its realization that it lives or dies because of its success in the local market. It has no other businesses or markets to dilute its interest or potentially subsidize its customer base.

The current FCC rules provide for the selection of licenses via a lottery process if there is more than one applicant. In Hawaii there will be one applicant for each of the three wireline (or telephone company) licenses, for the three RSA's. As an affiliate of Hawaiian Telephone, GTE Mobilnet will probably receive the licenses from the FCC without difficulty. The non-wireline licenses, which will be sought by Honolulu Cellular, will be more problematic.

Recently the FCC has been inundated with applicants for non-wireline licenses. Hagerstown/Cumberland, Maryland received approximately 3,200 applications. The vast majority of the applicants today are speculators who have no intention of building cellular systems. Generally these speculators in

01/26/88 10:52 HONOLULU CELLULAR TELEPHONE CO.

the smaller markets have sold the licenses to the carriers in the neighboring metropolitan markets. Conservative market pricing for these licenses is about $20 a unit of population in the licensed area. Some areas have gone as high as $30 to $40 a head. For example, Maui County with a population of 83,500 (1984) could cost Honolulu Cellular about $1,600,000 before even starting construction. GTE Mobilnet, based on an automatic transfer of the license from Hawaiian Telephone (which some would argue should result in compensation to the Hawaiian Telephone consumer rate payer), would incur no such start-up cost.

Benefit To Neighbor Islands

By adopting several changes to the FCC rules for accepting applications for cellular licenses, Congress can insure that service which is very much needed on the outer islands can be quickly provided. This service will increase the productivity of local business allowing Hawaii to be much more competitive with the world in the provision of goods and services. Cellular service will also enhance safety and security for neighbor island residents.

Honolulu Cellular on Oahu has shown the value of competition in providing communication services in advance of its competitor. Without a legislative solution to the present FCC rules for applications, cellular may be delayed another two years as negotiations for purchase of licenses from speculators slow the implementation by Honolulu Cellular and by extension, GTE, into the outer islands.

The existence of an operating switch in Honolulu will negate the requirements for separate switches on each of the neighbor islands and will unify operation of phones so that customers will have the same dialing patterns and features regardless of which island they are on. Each switch can cost hundreds of thousands of dollars. Honolulu Cellular's represent a $2 million investment.

The final benefit to adopting changes to the FCC rules will be in pricing to residents of Hawaii. If speculators are allowed to benefit to the tune of several million dollars for the sale of licenses to Honolulu Cellular, clearly the costs will be ultimately borne by the customer. In eliminating speculative applications, consumer costs will be minimized.

Proposed Legislative Solutions

The legislative solution to this situation can be summarized by the following points:

1. Limitation of non-wireline applicants to current adjacent MSA licensee and to the RCC licensees providing service in the RSA to be applied for.

This guideline will immediately eliminate the speculator but include the applicants best able to implement and operate cellular service on the neighbor islands.

2. Refinement of the definition of "adjacent MSA" to include Oahu as the adjacent MSA to Kauai, Maui, and Hawaii Counties, which are the three MSA's.

On the mainland no such unique situation exits, but in Hawaii the existence of the Pacific Ocean between counties serves to confuse the notion of adjacency. By operating off the existing switch on Oahu, service to the neighbor islands would be less expensive and more efficient.

Because of the scheduling of the hearing before the Senate Commerce, Science and Transportation Committee on the morning of January 27, we must move quickly to air this local view before agreements are made which will move against the best interest of Hawaii's citizens.

Thank you for your assistance.

Mahalo for your assistance.

Respectfully submitted,

Glenn T. Umetsu
President & General Manager